IN THE SUPREME COURT OF NEW ZEALAND SC 76/2013

BETWEEN **RIDGECREST NZ LIMITED**

Appellant

AND **IAG NEW ZEALAND LIMITED**

Respondent

Hearing: 10 March 2014

Coram: McGrath J
William Young J
Glazebrook J
Blanchard J
Tipping J

Appearances: C R Carruthers QC and P A Cowey for the Appellant
B D Gray QC and P M Smith for the Respondent

CIVIL APPEAL

MR CARRUTHERS QC:

May it please Your Honours, I appear with Mr Cowey for the appellant.

McGRATH J:

Mr Carruthers, Mr Cowey.

MR GRAY QC:

May it please Your Honours, I appear with the respondent and with me Mr Smith.

McGRATH J:

Mr Gray, Mr Smith. Mr Carruthers? Can I just say we thought 11 am might be when we need a cup of coffee this morning with this rescheduled timing?

MR CARRUTHERS QC:

I'm content with that Your Honour thank you. Your Honours, may I begin by just drawing attention to the terms of the preliminary question that was before the Courts. It's at page 70 of the case on appeal. The deliberate focus of the questions is on the proper interpretation of the policy. Just purely an interpretation question. There are obvious factual issues that are really pated from the questions themselves and that is more clearly so from the agreed statement of facts and that's at pages 67 and 68 of the case of the agreed statement of facts. If I can just say a word about the purpose of the agreed statement because it came in for some criticism from the Court of Appeal. What the parties endeavoured to do was to set out their respective positions where there was agreement that's reflected where there is a difference, the difference is recorded, just simply so that the Courts below had some guide as to what the meets and bounds of the factual issues were but the focus is certainly just on interpretation of the policy.

So moving from the preliminary question I want to go to the issue of interpretation of the policy and if I can take you to my written argument, I'm at paragraph 10 where I have summarised the effect of the policy. I've noted that during the period of insurance, and that's a year, the business assets, and I'll come back to that, if the appellant were insured by the respondent. The business assets as defined by the policy was a commercial building in Christchurch. The limit in terms of amount for a claim, for one claim, was 1.984 million. The policy contained an option which had been exercised and which provided for replacement cover and importantly the policy specifically included loss or damage caused by earthquake. I've given you the reference

to the policy in the case and at paragraph 12 I've drawn attention to the cover that was provided by the policy and if I can take you to page 78 of the case, in the middle of that page there's a heading, "A, You are insured for." So it's sudden and accidental loss of or damage to your business assets, and the business assets are defined, at the top of the page, as including buildings. So what triggers the policy cover is sudden and accidental loss of or damage to the building that I have identified.

I can take you back to page 75 of the case and I've really set this out at paragraph 13 of my argument, please just delete the reference at the end of that quote, it's to the case on appeal in the Court of Appeal. I'm on page 75 of the case before Your Honours and the operative provision is under the heading, "The insurance," on the left-hand side of the page at the bottom, the second to last paragraph, "This policy covers only those parts for which a limit is shown in the schedule and the maximum amount you can claim under any part in respect of any one happening (inclusive of fees and costs) is the current limit for that part." And that takes us back to page 74 of the case in the schedule which is the business assets part, defines the business, defines the period, defines the situation, defines the limit as I put at 1.984 million, identifies replacement cover, deals with excess and deals with endorsements, and you'll see that that's the section that includes loss or damage by earthquake.

And the in paragraphs 14 and 15 of the argument I have set out the clauses that are in issue and they are at page 79 of the case and the relevant clauses are first C1, "This insurance will pay the amount of the loss or damage or the estimated cost of restoring your business assets as nearly as possible to the same condition they were in immediately before the loss or damage happened, using current materials and methods." So the crucial part of that clause is that it is an obligation to pay an amount and it is an amount which includes the estimated cost of restoring, so it's just to the as was condition, not an as new condition. And then quite separately, and in addition to the C1 clause, C2 provides for the replacement cover, "Where replacement cover has been agreed by us and specified in the schedule and following loss or

damage, you restore or replace the lost or damaged business assets, this insurance will pay for buildings where repairable, the cost of restoration of damage to the same condition when new, or if unable to be replaced because of such damage the cost of replacement by an equivalent building which meets your requirements at any site provided we shall not pay more than the cost of replacement at the site stated in the schedule," and it deals with the materials in the next section.

So the concept of C2 in the policy is that that provides for replacement but the obligation is on the insured to make the replacement. So the claim under C2 doesn't arise until the restoration or replacement has been made, and I'll deal with that in a little more detail. So what I've then done in my written outline is to summarise the essential features in paragraph 16 of the written submissions and there I've submitted that first, "The policy insured sudden and accidental loss of or damage to business assets. Business assets is defined as the commercial building insured under the policy. The policy provided a limit in respect of any one happening. A happening under the policy included earthquakes. The limit for any one happening was 1.984 million. Part C of the police sets out the amounts which can be claimed," and I've summarised C1. "The policy provided an option for replacement cover. That was exercised and accordingly replacement cover was available under the policy," and that is what C2 deals with.

Your Honours from that analysis of the policy I want to go directly to the appellant's argument which I have set out in section C, beginning at paragraph 20 of the written submissions. I have submitted that the argument can be stated quite shortly. "The argument was, and is, that in terms of clause C1 of the policy it is entitled to payment for the estimated cost of repairs to the same condition as before the damage caused by each of the four earthquakes." And I've submitted that that concept is captured in M A Clarke, *The Law of Insurance Contracts* (6th ed, London, 2009) and Clarke is in volume 1 of the bundle of authorities, and it begins at page 184, that's the title to the text, and the passage that I rely on is in the section on

page 186 dealing with the sum insured an independent loss. And on 187 on the –

TIPPING J:

Does the author feel any question of what happens if one loss is overtaken by another? Clarke?

MR CARRUTHERS QC:

No, no, but Your Honour that's the issue in this case.

TIPPING J:

Yes, well that's why I asked.

MR CARRUTHERS QC:

No, no –

TIPPING J:

He doesn't?

MR CARRUTHERS QC:

I come to that in a separate context but –

TIPPING J:

Yes I understand that but this particular author doesn't deal with that subject?

MR CARRUTHERS QC:

No.

TIPPING J:

No.

WILLIAM YOUNG J:

Well he deals with it only to the point that the cap doesn't apply.

MR CARRUTHERS QC:

In that sense that well the cap applies to each successive loss.

WILLIAM YOUNG J:

Yes, so you can collect more than you've insured for, according to the author?

MR CARRUTHERS QC:

Well, no, no, because what – no, that's the point.

WILLIAM YOUNG J:

No, no, but I think that's what he is saying, isn't it? If –

TIPPING J:

Well, that's your, in your favour, if that's what he's saying.

MR CARRUTHERS QC:

This is exactly in my favour, yes.

WILLIAM YOUNG J:

That's right. If the cap was $2 million in the situation the author is talking about, you can get –

MR CARRUTHERS QC:

Two million.

WILLIAM YOUNG J:

You can get more than $2 million –

TIPPING J:

You can get four –

MR CARRUTHERS QC:

Yes, I can. I can get successive amounts of $2 million, which is the point.

WILLIAM YOUNG J:

Yes.

GLAZEBROOK J:

But it's a cap per happening, that's why. It's not a total cap of insurance –

MR CARRUTHERS QC:

Yes, Your Honour.

GLAZEBROOK J:

– because if it was a total cap of insurance then this wouldn't apply.

MR CARRUTHERS QC:

No, that – no, with respect, I agree entirely. That's the whole issue in the case. So that's the origin of the passage that I've relied on. I've then submitted that under clause C2 the insurer only becomes liable to pay once the insured has restored or replaced the building damage and so becomes entitled to the increased cover for the cost of restoration to the same condition as new, and then I've noted that the appellant has no claim under clause C2 until that has been done. So under the policy, the only claim the appellant could make and has made is under clause C1.

Now – so the position is that the appellant is pursuing a claim under clause C1 at the moment. A claim under clause C2 remains open but only once the appellant has replaced.

So the concept is, and I'll explain this a little when I come to look at the way in which the policies have developed historically, the concept is that there will likely be a top-up of the C1 claims for the first three earthquakes on the appellant's argument, for the first two on the respondent's argument, but that all depends on a factual issue as to what the difference is when the replacement has been made. For the moment, all that is in issue is the C1 claim for the estimated cost of repairs, and let me just perhaps explain that a little by reference to the agreed statement of facts.

Let me go to page 67, and I'll deal with the first earthquake, and I'll deal with paragraph 3. The figure of 196,352 is the estimate of repairs made by the quantity surveyor engaged by the appellant. Now that's on a basis that that is to restore the building, the damage to the building, to the condition it was before the September earthquake. What I am dealing with in the analysis that I am making at the moment is that you have 196,000 here but once the building has been completed, the cost to restore that as new will likely have a buffer above that, and that is the C2 claim that can only be made once the replacement has been made. So that's the concept that we're looking at.

Now it might be helpful, having set out what the appellant's argument is, is to just clear away some of the issues which, in my submission, have misled the Court of Appeal into a wrong interpretation not only of the policy but what has in fact been done here, and in this respect the Court has made assumptions about the factual position without having the full facts before them, and I want to deal with the pleading issue first. If I can take you to the statement of claim which begins at paragraph 54, which begins at page 54. The policy is pleaded in paragraphs 3 through to 4.10, that's the first policy and in my submission that is correctly pleaded. It does not set out clause C1. It does draw attention to the existence of replacement cover in paragraph 4.7 but it is sufficient for pleading purposes, in my submission, that it pleads the policy. Now what is important at this point, is that at the time, at the time the proceeding was issued, no payment had been made to the insured at all so at the time the proceeding was issued, potentially the insured had a C1 and a C2 claim. The C2 claim, as I've said, depended on replacement but that the proceeding necessarily captured both concepts.

TIPPING J:

Well 4.6 appears to plead only the replacement cover provision. Now I do not think that necessarily binds you Mr Carruthers, because you can always amend but to be fair, that is what it appears.

MR CARRUTHERS QC:

I don't think a lot turns on the analysis of the pleadings that was made by the Court of Appeal because as we have noted in the argument, Your Honour, there can't be any possible prejudice to the defendant.

TIPPING J:

But I do not think anything much turns on the pleadings frankly, because this is a preliminary issue. The pleadings could change as we go along. And if this is not happily pleaded from present purposes, it can be amended.

MR CARRUTHERS QC:

Well I mean, and I have conceded it is not happily or fully pleaded and it really wasn't an issue that really, in my submission warranted attention for the purposes of the preliminary question, which is why I focussed on that to start with. The actual damage is pleaded in paragraphs 10 to 14 and just to clear away an issue there. We have focussed, in the argument on four earthquakes. You will see that this pleading pleads five. That really results from further engineering advice that was obtained after the proceeding was issued and there is an issue also concerning the status of the 13 June earthquake that I will clear away in a moment also.

BLANCHARD J:

But we do not have to get into any of that do we?

MR CARRUTHERS QC:

No you don't, no. No the questions are framed in a way that means you don't have to get into that. Then –

TIPPING J:

Could the answer to the questions though, depend upon which limb, C1 or C2 is actually ultimately an issue.

MR CARRUTHERS QC:

No because 4 –

TIPPING J:

Well I think this is quite important because in a sense, at least from my point of view, you are going to have to clear away the possibility that the answer may differ depending upon which ultimately becomes the operative claim.

MR CARRUTHERS QC:

No the sequence, Your Honour and this is really quite important. The sequence is that the insured is entitled to be paid the amount of the estimated cost of repairs, the moment that the happening occurs.

BLANCHARD J:

Whose estimate, Mr Carruthers?

MR CARRUTHERS QC:

It will –

WILLIAM YOUNG J:

Presumably that of the Court if necessary.

MR CARRUTHERS QC:

Well, it would ultimately – it would be an agreed figure.

BLANCHARD J:

And if there's no agreed figure?

MR CARRUTHERS QC:

Well, that's probably why ultimately we're – I see the point Your Honour is making.

BLANCHARD J:

Well, we really don't –

MR CARRUTHERS QC:

Well, I expect –

BLANCHARD J:

We really don't get into estimate, do we, because there is no estimate?

MR CARRUTHERS QC:

Well, there is an estimate.

BLANCHARD J:

Well, there are estimates but they're a range.

MR CARRUTHERS QC:

Well –

BLANCHARD J:

There's no agreement on an estimate.

MR CARRUTHERS QC:

Well, I expected from the insured's point of view, the insurer must at least be under an obligation to pay the insurer's estimated cost of repairs and there would then be an issue as to what was the proper sum of the estimated cost of repairs for which the insured would have to sue. But that – because there is an obligation under the policy to pay the amount of the estimated cost, if there is a dispute or an issue, at a minimum the insured must be entitled to the insurer's estimate.

WILLIAM YOUNG J:

Well, you could issue summary judgment. You could have issued summary judgment in October 2010 and said, "The estimate of costs which we – with a costable cost – the repair will cost $400,000."

MR CARRUTHERS QC:

Yes.

WILLIAM YOUNG J:

"We seek summary judgment for that." If the insurers have said, "No, they won't, they're going to cost 250," you can probably get summary judgment for the 250 –

MR CARRUTHERS QC:
Yes.

WILLIAM YOUNG J:
– with the rest left to swing.

MR CARRUTHERS QC:
For trial, yes, yes. So coming back to Your Honour, Justice Tipping, the – it is a stage process and that once replacement is made then the issue of the amount payable in relation to each of the four happenings is revisited because almost inevitably the replacement cost in relation to the four happenings will be greater than the estimated cost of repair. So, in my submission, it won't matter, it won't matter for the purposes of the question whether one's looking at ultimately a C2 claim.

TIPPING J:
Well, it might help if I say at least from my point of view I see this case as turning on whether the concept of merger stymies you from claiming four times.

MR CARRUTHERS QC:
Well, let me deal with that immediately. The concept of merger, I think as the cases, even the maritime cases, the marine claims recognised, depend on the terms of the policy. It's the policy that actually governs and in this case you have a liability that arises on each happening. So if you look at Lord Birkenhead's question, the answer to that is does the liability arise on the happening? And the answer is yes, and it's four yeses. Now the distinction is, in the cases that he was discussing, is that the conventional marine policy is a voyage policy and the issue of liability under the policy does not arise until the end of the voyage. So you can see that if you suffer damage under a

voyage, you suffer damage which would otherwise be insured under the voyage policy in the course of the voyage, then your ship gets torpedoed and sunk, the answer to that is that your liability, the insurer's liability under the voyage policy, is considered at the end of the voyage. So Lord Birkenhead's question is answered no in that case because the issue of liability cannot arise until the end of the voyage.

So my submission is that merger is just not a concept that arises in this case at all because of the terms of the policy, and leaves aside any issue about whether merger should be a concept or can be a concept in a material loss damage policy.

McGRATH J:
Now the *Wright, Stephenson & Co Limited v Holmes* [1932] NZLR 815 (CA) case you'll come to at some point, the suggestion in that case that Lord Birkenhead's observations had a wider application.

MR CARRUTHERS QC:
Yes, yes, and you'll understand in that case, Your Honour, that the case was answered by looking at the terms of the policy. The insured was arguing that it was a policy that provided for payment of an amount and on the terms of the policy, no, that wasn't so. It was to pay for repairs which could not be undertaken. So again you're looking at the terms of the policy, but I will – I come to deal with *Wright Stephenson*, yes.

WILLIAM YOUNG J:
Is part of the problem that the insurer set out to repair the building? Say the insured had simply said on the 5th of September, "Here's a cheque for $400,00," would it then have been arguable that when the building was written off the 400,000 had to be set off against the 1.8, 1.98 million? I doubt if it would be –

MR CARRUTHERS QC:
No.

WILLIAM YOUNG J:

– even though the effect is you would then have got 2.3 million.

MR CARRUTHERS QC:

Well, the potential, the potential is that I will get more than 1. –

WILLIAM YOUNG J:

Yes, I can understand this but –

MR CARRUTHERS QC:

Yes.

WILLIAM YOUNG J:

– what I'm – if they'd simply paid you out $400,000 –

MR CARRUTHERS QC:

Yes.

WILLIAM YOUNG J:

– on the 5th or 6th of September –

MR CARRUTHERS QC:

Yes.

WILLIAM YOUNG J:

– so with great celerity, and then the building is, say, a write-off after February or June, it would be hard to say the two events merged –

MR CARRUTHERS QC:

Yes, yes.

WILLIAM YOUNG J:

– because you've got two happenings –

MR CARRUTHERS QC:

Yes.

WILLIAM YOUNG J:

– you've got two separate covers, essentially each up to 1.98 million, and it's as it were, it's just a reset –

MR CARRUTHERS QC:

Yes.

WILLIAM YOUNG J:

– and the cover bites in again.

MR CARRUTHERS QC:

Yes. With respect, I agree, Your Honour, which is why I say in this case the concept of merger just cannot arise and I think it needs to be looked at very scrupulously as to what the policies provide, and you get that in the *Crystal Imports Limited v Certain Underwriters at Lloyds of London & Anor* [2013] NZHC 3513 case that discusses merger where right at the start it's recognised that that is not an event policy, so it's been discussed in an entirely different context from the context that we're looking at here.

TIPPING J:

What would happen, Mr Carruthers, if there were successive earthquakes, each one week later than the other? So in weeks 1, 2, 3 and 4 there are earthquakes. The first one causes 100,000, the second one 200,000, third one 300,000, the fourth one demolishes the whole building.

MR CARRUTHERS QC:

Right.

TIPPING J:

Your argument leads to the conclusion that you can get the accumulation of all those totals.

MR CARRUTHERS QC:

Yes, yes, it does, and it leads more than that, Your Honour. In relation to the 100, 200, 300,000, that's on a repair to the previous condition. This will all come down to a matter of evidence on being able to establish what, exactly what the damage was from time to time, but I still may potentially have under my replacement part an issue about what the as new position would have been for the 100, 200, 300 before I even –

TIPPING J:

But most people would say that your loss in those circumstances was the loss of the building.

MR CARRUTHERS QC:

But, Your Honour, that's where one falls into error because it's not a matter of indemnifying the insured for the insured's loss. It is for the sudden and accidental loss of or damage to the building –

TIPPING J:

Yes.

MR CARRUTHERS QC:

– and it is in relation to each event. So what I am doing, and all I am doing, is looking at what the policy says that I am entitled to.

TIPPING J:

Yes, and very skilfully, Mr Carruthers, but all I'm doing is testing the consequences.

MR CARRUTHERS QC:

Well, the consequences, Your Honour, are that I can get potentially, if my building was worth enough to start with, potentially I could get 1.984 million on each of the four occasions.

TIPPING J:
Yes.

MR CARRUTHERS QC:
Yes.

TIPPING J:
So your argument depends entirely really on the policy, as my brother Young says, resetting itself, if you like, after each happening and each happening is an individual claim which can never be overtaken by what happens later.

MR CARRUTHERS QC:
That's exactly so but I recognise the practical difficulty that I have is that I would have to establish what damage was done as a matter of fact on each occasion, which is why the quantity surveyor has been sent in after each.

TIPPING J:
But you resist any concept of earthquake one damage being overtaken or whatever word one chooses, merging in, earthquake 2's damage and so on. That is the crunch point in this case isn't it?

MR CARRUTHERS QC:
Yes it is because I can separate off, I can separate off factually the damage done by earthquake one from the damage done by earthquake two etc.

WILLIAM YOUNG J:
Say one half of the building fell over in the first earthquake but the second half of the building was fine. That would be a sort of simplistic version of the point you are making?

MR CARRUTHERS QC:

Yes, yes.

GLAZEBROOK J:

And you may decide not to repair, so are you saying that under clause 1 you can decide not to repair.

MR CARRUTHERS QC:

Yes.

GLAZEBROOK J:

If you decide that the second half – well actually the second half probably doesn't work in that circumstance but say you had a car and somebody went into the back of it and you decided that you could still drive it and you weren't going to bother repairing it. There is no obligation to repair, you are entitled to that money. And if later, somebody else, or if later there is an earthquake and the car is crushed in the building, then you get the replacement cost.

MR CARRUTHERS QC:

Yes.

GLAZEBROOK J:

That is the argument.

TIPPING J:

But if the value of the car is then diminished by your failure to repair.

MR CARRUTHERS QC:

Yes, yes.

McGRATH J:

But you have a contractual sum which you are entitled to be paid, for a total loss, regardless of residual value.

MR CARRUTHERS QC:

Yes, yes.

TIPPING J:

Is it possible that if the building had been repaired, it would not have been a total loss later?

MR CARRUTHERS QC:

No on the facts. On the facts, no. It is quite interesting if I can just take you, just very quickly. What happened on the 4th September earthquake, is that the parapet from a neighbouring building fell onto the insured building, fell onto the insured building and the roof and the lift shaft were damaged and temporary repairs were done to the roof. That's for September. Boxing Day, 26th December, the internal partitioning and some block work was damaged by the December earthquake, then in the February earthquake, 22 February 2011, the sheer walls in the building reacted correctly and absorbed all the force but that earthquake exhausted the capacity of the sheer wall so you finished up with sheer walls that required replacement and then 13 June all of that was overtaken because there was damage to the foundations of the building as a result of the June earthquake which meant that it became uneconomic to do a repair. Now there is an issue between the insurer and insured as between the third and fourth earthquakes. But just that thumbnail sketch gives you some concept of the discreet damage that was caused by the separate earthquakes.

WILLIAM YOUNG J:

Was the building occupied in February or not?

MR CARRUTHERS QC:

Yes it was, yes.

GLAZEBROOK J:

But not after February, presumably?

WILLIAM YOUNG J:

No because everyone was kicked out of the city.

GLAZEBROOK J:

Of course, yes.

MR CARRUTHERS QC:

Can I just take you to the question of the way in which this developed as a matter of fact, in relation to the first earthquake. Just so that you can appreciate what the insurer and the insured were doing. In the case, the documents that were before the Courts below, included the insurer's status notes and if I can take you to page 117 of the case. Now just work up from the bottom, please, and about the middle of the page come to the first reference to Fritz Muller in the left-hand column on the 8th of September at 10.29. Now that's the survey that's complete after the first – for the first earthquake.

Now the next relevant event is on page 116, and this works backwards through the pages, the second to last entry at 11 October 2010, "Insured called to inform that storm last night damaged temporary cover and requests permission to do more permanent repair until claim is settled." And there's a question of doing that repair, so that was an insured's repair.

Then in the middle of the page another Mueller entry, 30 November 2010, "Insured not happy with progress. Believes that Hawkins," who was the contractor engaged by the insurer, and I'll say more about that in a moment, "will drag process out longer."

Then 6 December, moving up the page, "Schedule of estimated costs sent to insured. Insured to submit proposal for cash settlement. Await his proposal."

And then, just so that we keep the sequence, let me take you to what that proposal was. If you just hold page 116 in the meantime and go to page 100, and this raises a question about who's in control of events under the policy,

you will see that the director of Ridgecrest is writing to the assessor for the insurer, “Further to our telephone conversation on Friday, we wish to confirm that as we have become aware that there is an option whereby we are not required to accept Hawkins as project managers for the repairs to our building, we have decided not to engage them in this capacity. Therefore we would like to finalise this claim with a cash settlement of $197,500,” which was roughly the – which was the insured’s estimate, “in full and final settlement of this particular claim.” So they were looking for settlement at that claim, and the response on – the response is recorded in the Mueller notes under 7 December, “Agreed with insurer that cash settlement is not an option,” and we’re still talking about the – Hawkins getting on with the work.

Now just hold there and go to page 101, which is the comment on the Ridgecrest letter at page 100, where internally what’s being said is, “I don’t know what they’re referring to in talking about them having an option to opt out of the Hawkins arrangement. IAG has contracted Hawkins to project manage all repairs and rebuilds. The insured has not been asked to engage them at all, we have.” Now I can leave the issue about the question of who does the repairs other than to say this, that this is not a policy that provides for the insurer to have the right to control the repairs. It’s silent on how the work is actually done, so there was always an issue right from the start about the control of those repairs.

Then just going to page 115, because you’ll see there’s a reference for – a reference to 30 March 2011, recommended payment of various invoices and reimbursement to insured. 20 April 2011, Hawkins claim, “Take out the lift repairs,” that’s been dealt with by a separate contractor, then 16 May the lift repairs are done and paid out and then 20 October 2011, working through the file to establish the cost of work leading up to the June earthquake. Now it’s not until – in fact the payments that are made are set out in the agreed statement of facts.

TIPPING J:

I'm having some difficulty understanding what point in this case this discussion is relating to Mr Carruthers. Is it –

MR CARRUTHERS QC:
Well what it relates to is the conclusion that the Court of Appeal said that this was a C2 claim and we only had a C2 claim when –

TIPPING J:
Oh I see.

MR CARRUTHERS QC:
When plainly the way in which the exchanges were going, we were asking for payment in relation to the estimated cost of repairs which can only be a C1 claim, apart altogether from the fact that the C2 claim can't arise until the insured develops the building.

BLANCHARD J:
But your more basic point is surely that the Court of Appeal should not have gone into questions of fact.

MR CARRUTHERS QC:
That's a point I've made in my written argument. That those facts are for trial which is why I opened this appeal by focusing on what the preliminary question was.

TIPPING J:
And your overriding point is it doesn't matter which head of C1 or C2, you're entitled. The amounts may differ –

MR CARRUTHERS QC:
Yes.

TIPPING J:

– but the concepts that we've been struggling with don't matter which route you go down?

MR CARRUTHERS QC:
That's right. One route, C1 can precede C2 and my proceeding is about both.

TIPPING J:
But you're saying that the concept of merger, for want of a better expression, doesn't bite whichever route you go down. Because that's really, I would have thought, the crunch point.

MR CARRUTHERS QC:
Yes it is. Yes. Well the starting point is actually to interpret the policy because my learned –

TIPPING J:
Oh yes, yes, I'm well beyond that. I don't see there are any great difficulties with interpretation here it's just the curiosity, if you like, that you've got a sequence of events, all within the same claims year –

MR CARRUTHERS QC:
Yes.

TIPPING J:
– that appear to be covered by, in effect, four separate covers if you like –

MR CARRUTHERS QC:
Yes, yes.

TIPPING J:
– but the only way I can see at the moment for the insurer to get round that is this idea of merger.

MR CARRUTHERS QC:

Yes, yes.

TIPPING J:

Now Mr Grey may have some other bright ideas but at the moment that seems to be the most promising one from his point of view.

MR CARRUTHERS QC:

Yes, yes. Well I'm content to meet that Your Honour. Can I just take you back through the written argument. The next section of the oral argument I want to make concerns the case in the Courts below, and I'm not going to dwell on this because I set it out quite fully in the written argument. I deal with the High Court judgment at paragraphs 25 through to 33 of the written submissions and essentially the Judge has agreed with the appellant's argument on interpretation of the policy, agreed with the appellant's argument on merge, but found that the contract was frustrated.

BLANCHARD J:

But is anybody arguing for frustration now?

MR CARRUTHERS QC:

No I don't think anyone's arguing –

BLANCHARD J:

So we don't need to get into that?

MR CARRUTHERS QC:

No, all I'm doing is, I was just pointing – no you don't need to get into frustration at all.

BLANCHARD J:

Because remember we have read this.

MR CARRUTHERS QC:

Yes.

TIPPING J:

It seemed a most unpromising proposition at the start. It's strange that it took some traction.

BLANCHARD J:

Well that is, yes, frustrated by the event it's insured against.

TIPPING J:

Yes.

McGRATH J:

And you'd have won in the High Court if the High Court Judge had seen it that way.

MR CARRUTHERS QC:

Yes, I'm very happy with an amalgam of the High Court and the Court of Appeal.

TIPPING J:

The good bits out of both.

MR CARRUTHERS QC:

Yes I'll have the good – yes it was a serious disappointment to lose frustration. And then – I won't take time because of Your Honour Justice Blanchard's comment, but I then set out what the argument was in the Court of Appeal and I've gone through the Court of Appeal judgment at paragraphs 45 through to 63.

Now – so having set out and taking Your Honour's lead, I can probably just capture my argument, and I think I have captured it already. My submission is that the Court of Appeal was wrong in its interpretation of the policy for the reasons that I've already canvassed in argument with you.

Can I just pick up some issues that arise, two issues particularly about what the entitlement is under policies, under event policies and generally under reinstatement policies, and I want to address an issue about the distinction between repair and reinstatement and the obligation to pay, and I do so because of the way in which the Court of Appeal has dealt with the argument on this issue, and I want to come back to the *TJK (NZ) Limited v Mitsui Sumitomo Insurance Company Limited* [2013] NZHC 298 case that I've cited in the course of argument. If I can just take you to page 36 of the case, and – I'm sorry, I want to go to page 20 of the case, my apologies. This is where the Court's dealing with the argument, "However Ridgecrest's counsel also argue the claim under C1 left open the possibility of a later claim under C2 which would arise if Ridgecrest proceeded to restore the damage. He argued that if a later claim were made under C1 IAG would then be liable to pay the difference between the amount it had paid to Ridgecrest under C1 for repairs on an old for old basis and the cost of restoring on a new for old basis, and then that reasoning goes through to paragraph 30 where that concept is elaborated on. I don't read the paragraph. And then that leads to the reasoning in paragraphs 42 to 44 which are on pages 24 of the case. 42, "Counsel argued, as he had in the High Court, that payment of the amount of a claim under C1 wouldn't necessarily resolve the insured party's claim. He said that a payment of the estimated cost of repair under clause C1 could then be followed by a claim for any additional cost of repairs under clause C2 in the event that an as new repair was undertaken by the insured party. There is nothing in the wording of the policy to support that proposition. And if it were correct, the converse would apply. If the insured party undertook the as new repairs and the cost was less than that paid under C1, presumably a refund would be payable. Counsel accepted that that would be so. That's a very unusual way of operating the policy, effectively creating an option on the part of the insured to undertake repairs on an overs and unders basis. It also affects the issue of what happens in circumstances where, as here, the repairs that Ridgecrest intended to undertake could not be undertaken because of the intervention of a further earthquake causing more damage. Counsel said the possibility of a refund would only arise where the repairs were actually undertaken and the cost of repairs was less than the estimate.

It did not arise in circumstances where the repairs could not be undertaken because of a supervening event such as a further earthquake. There is no particular logic to that position and it calls into question the concept of a provisional resolution of the claim under C1 followed by a top-up or refund under C2."

Well, with respect, those paragraphs demonstrate a fundamental misunderstanding of the policy and, more importantly, a fundamental misunderstanding of what the law is in relation to the relationship between a repair and a replacement policy and the obligations under each and that's why I have cited the *TJK* case. So there is nothing in the wording of the policy to support that proposition. Well with respect, there is everything in the policy to support that proposition. Not only does the policy follow the law but the policy is plainly capable of that.

WILLIAM YOUNG J:
Well it actually says it doesn't it?

MR CARRUTHERS QC:
Mhm?

WILLIAM YOUNG J:
It actually says it. It seems to me that it is as though the word "not" has been missed out. Because the policy says they are to pay and it does put the onus of reinstatement and repair on the insured.

MR CARRUTHERS QC:
But this refund concept, it was put to me. If the new was less than the old for old, then there would be a refund. Well obviously I was driven to concede that but the logic was wrong because it would be remarkable if ever an old for old was less than an as new. So the proposition that I was putting, the proposition that has been picked up there of overs and unders, was simply in answer to the Court on a proposition it was unlikely. Now let me go to *TJK*, Your Honours there is a supplementary bundle that we put in. *TJK* had been

left out of the original bundle; it's the first in the supplementary bundle and if I can just explain what was being done by Miller J in that case. You will see in my written outline at paragraph 52, I have referred to paragraphs 28 to 34 of *TJK*, where Justice Miller just analyses the policy and I will leave you to deal with that. I really want to come to his conclusion at 42 to 44 and look at the way in which the general law provides. And he says at 42, "I hold that the earthquake reinstatement extension in Mitsui's policy, expressly recognised that indemnity value might be payable in some circumstances and further that it might be payable before TJK incurred reinstatement costs. Put another way, the extension provided for payment of both indemnity value and the difference between indemnity value and reinstatement costs. The latter sum, the difference is what the extension meant by the cost of reinstatement. Because reinstatement cover was an additional extension to the primary indemnity, applicable only where the insured chose to repair or rebuild, the insurer's obligation to pay reinstatement costs, would arise only as the insured incurred such cost. The rationale cannot effect the obligation to pay indemnity value which compensates the insured for a loss suffered when the building was damaged. The insured need not put a payment for indemnity value to any particular use, in particular it need not reinstate the property. The policy did not provide expressly that where the insured elected reinstatement, the insurer must pay indemnity value on proof of loss. But such a term would be redundant. The obligation to pay was effected only where the insured elected reinstatement and only to the extent that reinstatement would compensate the insured for a loss depreciation for which it would not otherwise be indemnified at all. And that is the legal position – is actually historically correct.

If I can take you to *Brkich & Brkich Enterprises Limited v American Home Assurance Co* (1995) 127 DLR which is in volume 1 of the authorities. It is authority number 10 and it begins at page 188 of the volume and I am taking you to the discussion beginning at the bottom of 195 and there are two passages I just want to read to you, 195 at paragraph 27. "Replacement costs or depreciation insurance is a relatively recent development, quite unknown when *Castellain v Preston* (1883) 11 QBD 380 was decided. Useful analyses of replacement cost policies are found in the reasons for decision of

the Supreme Court of Oregon in *Higgins v Insurance Company of North America 469 P.2d 766 (1970)* and in an article by Mr Jordan, what price rebuilding. Both of these discussions describe the historical development of replacement cost insurance. It began with recognition that an insured under a pure indemnity insurance contract, which pays only the cash value of the property at the time of the loss, would not receive sufficient funds to restore the property's pre-loss use." The property's owner dilemma was well described by Higgins and I can leave Your Honours to read that.

Just going to page 29 on page 197, "Replacement cost coverage was first offered as separate additional coverage of depreciation and later in combination with the actual cash value insurance, as an original endorsement," and there's a reference to *Carlyle v Elite Insurance Co* (1986) 25 DLR (4th) 740 (BCCA). Replacement cost insurance raises concerns of increased moral hazard because it creates the potential for an insured to obtain more than mere indemnity for the damaged property. To address this concern insurer is willing to offer a replacement cost, have typically limited their obligation to pay more than the actual cash value to circumstances where reconstruction was actually carried out as described above by Mr Jordan. So you can see that Justice Miller's analysis has a sound historical base. The other concept that I just want to draw attention to is the law relating to the application of payments made under a policy and in that additional bundle, Your Honours there is another extract from Clarke on reinstatement. It's the last of the authorities, sorry I want to deal with them in this order. And in dealing with reinstatement and the introduction in s 29-1, the author footnotes this reference as footnote 1. "If the insurer pays insurance money to the insured, the insurer cannot require the insured to spend the money in reinstatement of the property." And you will see that that cites a case called *Reynolds v Phoenix* [1978] 2 Lloyd's Rep 440 which is in the bundle. It is in volume 1 it is authority number 12 and it begins at page 21.

TIPPING J:

Presumably that is the foundation for the practice, to make reinstatement a precondition of recovery. The actual reinstatement.

MR CARRUTHERS QC:

Yes, yes the insured has to actually do it.

TIPPING J:

Has to actually do it as well as the moral hazard issue.

MR CARRUTHERS QC:

Yes the provision meets the moral hazard issue.

WILLIAM YOUNG J:

Well not entirely because they still get a better building.

MR CARRUTHERS QC:

Well yes.

TIPPING J:

It is more tempting to burn your house down if you are going to get a new house than a patched up house. That's the moral hazard.

MR CARRUTHERS QC:

And that's actually the moral hazard that's in *Reynolds* that I am about to cite to you. Just go to page 213 and you will see the three questions that were before the Court. So there's a lengthy judgment and it is not until the issue of the impact of the Fire Prevention Metropolis Act 1774 is considered, that this issue arises and I just take you to this passage to support Clarke. It is at page 233 of the bundle of authorities and there is a discussion there in the implications of the Act.

BLANCHARD J:

This is not affected by the fact that that Act has been repealed in New Zealand.

MR CARRUTHERS QC:

No, no, it doesn't, Your Honour. All I'm citing it for is in the left-hand column, in the last substantive paragraph, there's a proposition just of law, that is, "An insurance company giving fire cover is bound under the contract to pay the insurance money to the assured. If it does so, the assured is quite entitled simply to put the money into his pocket without in any way reinstating the building," and in *Colinvaux* –

GLAZEBROOK J:
Sorry, I think I've just – no, I've found it, sorry.

MR CARRUTHERS QC:
I'm sorry, Your Honour. *Colinvaux* is to the same effect at paragraph 10-049, that's the middle authority in that additional bundle, "Where at common law an assured who has been paid the proceeds of the policy by the insurer is not under any obligation to apply the proceeds to reinstating the lost or damaged subject matter. He may do so. He may do as he pleases with any sums received by him," and then the author goes on quite properly to say the position may of course be varied by contract between the – the contract with the assured.

So just that's really in the face of the way in which the Court of Appeal has dealt with it, and also there was a suggestion in the Court below of windfall, but the position is that the insured can deal with the C1 payment as he wishes but obviously the construct of the policy, as Justice Miller notes in *TJK*, is that the insurer pays the initial payment so that that can fund the insured to commit to replacement and then get the benefit of the replacement issue – replacement, the replacement cover.

Now, Your Honours, I want to turn now to the additional arguments I made on merger and Your Honour, Justice McGrath, asked me if I was going to deal with the *Wright, Stephenson* case and in that – I am at paragraph 65 through to 83 of my written argument where I deal with the argument of merger, which is really based, my argument is based squarely around the policy meaning and all of the cases recognise that it's the policy meaning that dictates.

If Your Honour has a particular question about *Wright, Stephenson* in addition to the analysis that I have made in that section, I am content to deal with it, but my written submission does cover the argument on that point.

McGRATH J:
All I was concerned was the view that there was a broader application of what Lord Birkenhead was saying. It seemed to me to be a significant aspect, the broader application reaching beyond instants of marine misadventure to general insurance policies.

MR CARRUTHERS QC:
I expect if you had a general policy that had the same concept as a marine policy you may well get to the same position, but bear in mind a material damage policy will trigger liability on the occurrence of loss or damage.

McGRATH J:
Yes.

MR CARRUTHERS QC:
So Lord Birkenhead's question is immediately answered "yes" and not "no". Now if you had a conventional policy that was structured so that all claims would only be considered at the end of the policy period, you would have the equivalent of a voyage policy in marine insurance, and one can see that if the trigger date for the question was the end of the period of cover then you would conceivably have a merger argument if you had successive events in the course of the period of cover.

McGRATH J:
So I think what you are saying Mr Carruthers is that you have no problem with the Court of Appeal's observation that Lord Birkenhead's remarks can be given wider affect. But what you are saying is, it has to be in connection with the same structure of policy.

MR CARRUTHERS QC:

Yes, yes Your Honour.

McGRATH J:

Of which Lord Birkenhead was talking about.

MR CARRUTHERS QC:

Yes that is my analysis, yes.

TIPPING J:

Is that your essential point in distinguishing marine policies from other policies, this end of voyage point?

MR CARRUTHERS QC:

Yes, it is.

TIPPING J:

Is there any case of which you are aware and I am sure it would be in here if you had found one, which expressly deals with the point that you shouldn't extend the marine approach to more general insurance?

MR CARRUTHERS QC:

Well I think that was Justice Dobson's approach.

TIPPING J:

Well other than the one under appeal.

MR CARRUTHERS QC:

I just commend it to Your Honour. No, no I don't –

TIPPING J:

Do the text book writers touch on the question of whether the marine approach should or should not be applied more generally? I assume not otherwise you would have referred to.

MR CARRUTHERS QC:

I don't – I am hesitating because I am not quite sure what my learned friend has turned up more recently than me. No I don't think there is. Your Honour there is nothing that I found that I haven't drawn to your attention.

WILLIAM YOUNG J:

So really the key point for you and this is not a net loss at the end of a period.

MR CARRUTHERS QC:

No.

WILLIAM YOUNG J:

This is a loss by loss policy.

MR CARRUTHERS QC:

Yes, an event by event.

WILLIAM YOUNG J:

Event by event, that's the key distinction.

MR CARRUTHERS QC:

And that's the distinction between this case and *Crystal Imports Limited* that Justice Cooper decided, right from the start, he notes that that is the distinction.

WILLIAM YOUNG J:

Where does the actual cap appear in the policy, is it actually in an email, I am just looking through the policy. It is not expressed to be the replacement value of the building, it is just a limit on the ability on the liability of the insurer to pay out per event, is that right?

MR CARRUTHERS QC:

Yes it is, it is simply in the schedule.

WILLIAM YOUNG J:

I am sort of struggling to find it in the schedule. It may be that it has been changed, there is something on page 82.

MR CARRUTHERS QC:

If you go to page 74. You have got the schedule there and the business assets – these are the words that appear in that operative provision on page 75, "As policy cover for only those parts, for which a limit is shown in the schedule."

WILLIAM YOUNG J:

Presumably the marine cases did not have insurance caps that operated like this. There would presumably have been an in substance cap being the value of the ship, which was the total insured.

MR CARRUTHERS QC:

Or cargo if it was a cargo policy. Yes my friend has just commented to me correctly that they usually value the policies, so they are dealt with in that way.

WILLIAM YOUNG J:

So that the ship would be expressed at a particular value.

MR CARRUTHERS QC:

Yes.

WILLIAM YOUNG J:

So it is a different sort of cap from the one that is here.

MR CARRUTHERS QC:

Yes it is.

GLAZEBROOK J:

I was wondering whether you were going to take us through those marine cases in some more detail, just to indicate why they are dependent on that, which can be after the break if you want to.

TIPPING J:
Yes I, too, would be helped by anything said by Lord Birkenhead or anyone else of authority in this field, suggesting that it is the net loss at end of period approach is what takes you to the merger situation.

MR CARRUTHERS QC:
Right.

WILLIAM YOUNG J:
Well, possibly the point is that if there wasn't a merger then the insured would get more than had been lost.

MR CARRUTHERS QC:
Yes, yes, you –

WILLIAM YOUNG J:
Whereas in this case the insured doesn't get more than was lost.

MR CARRUTHERS QC:
That's –

WILLIAM YOUNG J:
It may be as simple as that…

MR CARRUTHERS QC:
Well, it is and I think that the *British and Foreign Insurance Co Limited v Wilson Shipping Co* Limited [1921] 1 AC 188 case which –

GLAZEBROOK J:
Sorry, why is there not more than is lost in this one?

WILLIAM YOUNG J:

Because here it's a – there is not a – the cap is not a purported value of the building.

GLAZEBROOK J:

No, so event by event?

WILLIAM YOUNG J:

So it's event by event, so –

GLAZEBROOK J:

Yes, I understand. No, I was just…

MR CARRUTHERS QC:

I'll take you to *Wilson* which begins at page 33, and the passage from Lord Birkenhead. I've referred, if I can – the first reference I've made, and I'm looking at paragraph 72 of my written argument, is at 195 of the report on page 36 of the bundle, and it's right at the top of page 195. Well, perhaps I'd better go to the bottom of 194 so you can pick up what the principle is. *Stewart v Steele* (1842) 5 Scott, N.R. 517 was a case in which *Livie v Janson* (1810) 12 East 648 was cited and discussed both during the argument and in the judgment. Justice Maule in the course of his judgment stated the fundamental principle that the proper time to estimate the loss where the party is put to no expense is at the expiration of the risk. This principle underlies the decision of Lord Ellenborough for as Justice Maule in an earlier passage on the same page says, "It is said that the plaintiff had a vested right of action at the moment of the happening of the loss which nothing could afterwards divest. That I apprehend is quite contrary to the doctrine laid down by Lord Ellenborough in *Livie v Janson*. The learned Judge was of the opinion that in as much as the time for assessing unrepaired damage is at the expiration of the risk if the vessel is totally lost before the risk expires, there is nothing upon which such assessment can be made." And then that's picked up at 198 to 199 by Lord Birkenhead, and this is a discussion of all of the

authorities and it goes for some pages, and if I pick up the passage that – where His Lordship starts discussing the cases at 196. I mean, he's discussed previous cases but then comes on to the key cases. "The next case of importance is *Lidgett v Secretan (No 2)* [1871] Law Reports 6 CP 616 decided by Justice Willies. In that case while a ship which had suffered partial damage was being repaired, the policy –

McGRATH J:
Sorry, what page are you on?

MR CARRUTHERS QC:
I'm on page 37 of the bundle of authorities and 196 of the –

McGRATH J:
Thank you.

MR CARRUTHERS QC:
– report in *Wilson*. "In that case, while a ship which had suffered partial damage was being repaired, the policy expired and shortly afterwards, before the repairs could be completed, she was totally destroyed by fire. During the argument, the learned Judge remarked that the reason for applying the doctrine of merger where the partial loss and the total loss occurred during the continuance of the same risk is obvious. The parties never intended that the insurer should be liable for more than a total loss in any event but the same reason does not apply where the partial loss takes place during the period covered by one policy and the total loss whilst the ship is insured for a different voyage and under another policy" and in his judgment he reverts to this topic and comments on *Livie v Janson*. There is another case, namely where after the vessel has sustained damage, but has not been repaired and has subsequently and during the currency of the policy being totally lost by a peril accepted out of the policy and in respect of which the owner was his own insurer. Such was the case in *Livie v Janson*. Mr Wright admitted that if this passage were good law, then the respondents must fail but he contended that the dictum was wrong. It is not necessary in this house to insist upon the

respect which is due to any considered opinion of Justice Willes. Justice Lindley in *Pitman v Universal Marine Insurance Co* (1882) 9 QBD 192 CA made a pronouncement to the same affect as that of Justice Willes and Mr Wright also admitted that if this opinion was in law well founded, the respondents in this case are wrong. *Pitman's* case turned upon the question, what is the true principle upon which an unretired loss is to be estimated. In the course of his judgment, Justice Lindley remarked, "Against what do the underwriters agree to indemnify the assured, certainly against such loss as he may in fact sustain by reason of the perils insured against. That is so is plainly proved by those cases which decide that where a ship has been injured and not repaired, the assured must wait until the expiration of the risk before he can sue the underwriters for the loss he has sustained. The assured has no vested right of action when the injury is sustained. If in such a case the ship is lost whilst the policy is running by a peril not insured against, the assured has no right of action at all and if she is lost by a peril insured against, the assured can only claim for a total loss. He cannot claim both. The judgment of Justice Lindley was upheld by the Court of Appeal with a variation which is not relevant to this part of the judgment. The authorities establish the existence of a rule whereby underwriters are not liable for unrepaired damage if there is a total loss before the expiration of the policy." As stated by Lord Ellenborough in *Livie* and by the Court of Queen's bench and Knight the rule might appear to be limited to the case where the previous deterioration became ultimately a matter of perfect indifference to the assured's interests. Justice Bailhache adhering to the view expressed by Justice Willes and Justice Lindley, in the cases cited came to the conclusion that there was no such limitation. The Court of Appeal on the other hand, having regard to the statement of the rule by Lord Ellenborough and Lord Campbell were of the opinion that the condition was an integral part of the rule and that therefore the present case was in all facts distinguishable from *Livie*. If Lord Ellenborough's words are taken to mean that the circumstance, more than once, and somewhat pointedly insisted on, is a condition to the application of the rule, the Court of Appeal may well have been right in the distinction which they drew. I have, however, come to the conclusion that no such condition ought to be admitted. Lord Ellenborough was dealing with

unusual facts and his judgment must be construed in relation to those facts. But the rule ought not be limited in the manner suggested. I adopt the reasoning of Justice Bailhache in the following passage in his judgment. "Whether an underwriter is or is not liable for unrepaired damage, cannot be ascertained until the expiration of the policy. If before the expiration of the policy there is a total loss, he is not liable to pay for the earlier unrepaired damage, sustained during the currency of the same policy and it makes no difference whether the total loss falls upon him or is due to an accepted peril against which the owner is insured or uninsured. The true doctrine is that the smaller mergers and the larger, and the rule is not limited to the ground upon which it was based by Lord Ellenborough, namely that there was no continuing prejudice. The question in every case must be did the total loss happen before the underwriter's liability for the unrepaired damage accrued. If yes he is not liable, if no, he is liable. It would be strange if an underwriter's liability should vary with the terms of some contract, not needing to be disclosed to him which the owner has made with some stranger to the contract of insurance."

I think I probably don't need to read any more than that but does that assist Your Honour with the way in which those marine cases have worked because that is Lord Birkenhead really traversing the issues and coming to the question that is the yes or no question on when the liability arises.

WILLIAM YOUNG J:
Your argument is that under C1, liability accrued on each event?

MR CARRUTHERS QC:
Yes it is.

TIPPING J:
And it could be said that it is difficult to reconcile the marine rule with an event by event policy?

MR CARRUTHERS QC:

Yes.

TIPPING J:

Because that type of construction, if you like, or scheme of policy, obviously is the antithesis of a "wait until the end of the risk"?

MR CARRUTHERS QC:

Yes, yes.

TIPPING J:

I am thinking aloud Mr Carruthers but that is the point of some force.

MR CARRUTHERS QC:

Yes and that, when Justice McGrath asked me about the *Wright Stephenson* case and asked me to provide an example of where it might apply. You would have to have a policy constructed like a marine policy.

GLAZEBROOK J:

Can I just check if this – under clause 1 and say there wasn't a replacement option at all, presumably you can either take the money and not repair or you can take the money, repair and then if there is a difference, claim the difference under clause 1 as well, in terms of a reinstatement to old, or as current condition.

MR CARRUTHERS QC:

Yes and so in terms of that analysis that Justice Miller makes, the insurer would pay an indemnity, the actual loss that had been suffered under a repair policy.

GLAZEBROOK J:

And you would actually be; because say you had a whole lot of cumulative accidents that you decided not to repair. So you are driving along in your very rickety car by this stage and you decide not to repair each of them, then, in fact, you are providing a total cover if you applied the marine cases. You

would be applying a total cover, so say you had an accident, actually it's a car so a $1000 per accident and you had five accidents of a $1000. Well if you applied the marine, you would actually land up only with $1000 on this analysis, wouldn't you. On the marine analysis because you would look at the end of the year and treat it as not an event by event limit but as a total limit.

MR CARRUTHERS QC:

Yes that would be right because you would have to look at the end of the risk period, what the damage was.

GLAZEBROOK J:

So conceivably you could have to pay something back under that. Say your car is written off at the end of the period, you could conceivably have to pay some of the money back that you have already taken, if you do apply the marine policies, the marine insurance.

MR CARRUTHERS QC:

But they would presuppose you had been paid on the way through though.

GLAZEBROOK J:

But you had a right to be paid on the way through and you claimed on the way through.

WILLIAM YOUNG J:

Under the marine policy you don't have a right to be paid on the way through, that's what they are saying isn't it?

GLAZEBROOK J:

No but that's what I said. That if you did apply it to the other type of policy, conceivably you could land up having to pay something back even though, in fact, on a per event basis you were allowed to claim those amounts.

MR CARRUTHERS QC:

Yes.

GLAZEBROOK J:

And not repair. Both of which seem to be not the case in the marine context.

TIPPING J:

So you mean you get $5000, five times a $1000 and your car at the end is only worth $4000, so you have to pay back $1000.

MR CARRUTHERS QC:

Your Honours –

GLAZEBROOK J:

A car was an easy one.

McGRATH J:

Are you heading for a new point Mr Carruthers?

MR CARRUTHERS QC:

I am but I am really going to simply say that I have dealt with the argument on implied term in my written argument, I haven't got anything to add to that and if I might just read my summary Your Honour, I can conclude my argument at that point. So what I have submitted at paragraph 87 is the starting point, is to recognise that the cover under the policy extended to loss or damage caused by earthquake and that cover up to the limit under the policy was available for each happening. Accordingly, the parties recognise specifically that there was an insured liability for each earthquake up to the limit for each earthquake. There is no limit to the number of earthquakes covered during the period of insurance, and the High Court Judge's decision may be tested by asking what the outcome would have been if there had been sufficient time between each happening for the assessed repairs to have been carried out. Plainly the appellant would have been entitled to payment in relation to each happening in accordance with the policy. In each case, whether the repairs have been carried out or not, the damage and the estimated cost of restoring are all the

same. So I've submitted there's no reason in logical principle to distinguish between the two situations postulated.

Your Honours, unless you have questions, those are my submissions in support of the appeal.

McGRATH J:
Thank you, Mr Carruthers. We'll adjourn for 15 minutes.

COURT ADJOURNS: 11.01 AM
COURT RESUMES: 11.17 AM

McGRATH J:
Mr Gray.

MR GRAY QC:
Thank you, Your Honour. May it please Your Honours, we take issue with our learned friends. We, like His Honour, Justice Tipping, really say merger is the key to this case and that all other parts really come back to there, that there is a common analysis which underlies the different doctrinal solutions that might be available.

McGRATH J:
Yes.

MR GRAY QC:
But what has to be grasped is whether merger applies or not.

McGRATH J:
Yes.

MR GRAY QC:
With respect to our learned friends, we disagree with them entirely about how marine insurance works. We don't accept for a moment that in the course of a

marine policy if an incident, an event, occurs which gives rise to a claim, for example, for repairs to a vessel, then those repairs can't be undertaken immediately and an obligation to pay for them does not arise immediately. What happens in marine insurance, of course, is that sometimes repairs can't be undertaken immediately because the vessel is at sea, and so the repairs are deferred until the vessel gets to another port and sometimes the ship can sail without the repairs being undertaken and they don't get repaired till later and in those circumstances, in marine insurance, if at the expiry of the policy period the repairs have not been undertaken then the measure of loss is the diminution in the value of the vessel between its value with and without the repairs, but we have in our synopsis addressed that proposition. We have shown that we say –

WILLIAM YOUNG J:

That's not that – that's just only slightly different from what he was saying. Isn't the position that in the case of an unrepaired vessel, the liability of the insurer is only crystallised at the end of the policy?

MR GRAY QC:

Not necessarily, Your Honour. It's crystallised at the time the repairs are undertaken. Well –

WILLIAM YOUNG J:

Well, that's not quite the way Lord Birkenhead explained it.

MR GRAY QC:

We'll go back to them, Your Honour, because those passages need to be read carefully. They are all begun with, "In the case of an unrepaired vessel."

WILLIAM YOUNG J:

Yes, well, that's what I'm saying.

MR GRAY QC:

So it's in those circumstances where the repairs are not undertaken.

WILLIAM YOUNG J:

Can I just ask you one thing, what – the policy doesn't really give the insurer a right to do repairs.

MR GRAY QC:

Well, it's silent. It's one of these modern policies that's written in – with the –

WILLIAM YOUNG J:

So what was the – had –

TIPPING J:

Has all the virtues of plain English.

WILLIAM YOUNG J:

Yes, but had the insurers just done what the insured asked and paid out after the first event, this argument wouldn't have got off the ground, would it?

MR GRAY QC:

No. If an amount had been paid, then that first claim would have been deal with.

WILLIAM YOUNG J:

Yes, and your –

MR GRAY QC:

What mergers –

WILLIAM YOUNG J:

But what puzzles me a little is how your client's insistence on doing the repairs itself over their protests changed their entitlements.

MR GRAY QC:

Well, Your Honours, with respect, we do have to be practical about what was happening in Christchurch. There was a lot of damage, there was enormous demand for services. It was the large insurers who could contract the large construction companies and say, "Please do as much work as you can. Please prioritise it as you can. Please get it done as you can."

WILLIAM YOUNG J:
But they couldn't. They're not entitled to do that in breach of contract, are they?

MR GRAY QC:
Well, it's not in breach – well –

WILLIAM YOUNG J:
Well, that's an issue because it's just a preliminary question so we don't know, but on the face of it they're saying, we don't want Hawkins to do it. We want you to pay us out.

MR GRAY QC:
Yes. Your Honour is quite right. This is not one of those policies that says, if the parties agree then in the event of damage it's the insured who has the right to engage the builders and to do the repairs.

WILLIAM YOUNG J:
Well, no, that's exactly what it says. The insured has the right to do it.

MR GRAY QC:
Well, we'll –

WILLIAM YOUNG J:
It thought that's what it says.

MR GRAY QC:

– come to the policy, Your Honour. It's – well, let's start by going to the police. It's at page 74 of the case, Your Honour. It starts with the schedule. As Your Honours have already seen, the business asset parts are defined and the limit, and the extension in the endorsements to cover by earthquake.

Over the page at 75, in the bottom left-hand corner under the insurance, the underwriter is identified and it agrees to provide the insurance set out in the policy. It is not itself the operative clause. That is not the clause that provides the insurance. It says, "We'll give you the insurance that's in the policy." It goes on to say, "You only have cover for the bits for which a limit is shown in the schedule," and it's a limit, as Your Honour noted in an exchange with my learned friend, per event. Nothing on 76 but on 77 are the conditions, and I draw Your Honour's attention to 4. "Unless we have agreed, you must not incur any expense or admit liability in connection with the claim." When the repairs are undertaken they've got to be done together. You can't go away and spend money unless we've agreed.

WILLIAM YOUNG J:
But they can't not agree if it's reasonable, can they?

MR GRAY QC:
Well that's the second phase, with respect Your Honour. The policy is we have to agree the repairs.

WILLIAM YOUNG J:
Well what about C1?

MR GRAY QC:
Well can we get to that Your Honour. We then get to page 78 and before we get to C we start with A. So the question is, what are you insured for, and here is the operative cause. Sudden and accidental, loss of or damage to your business assets, so that is what the insurance is about. It is about loss of or damage to business assets. Not sums of money. B1 is the exclusions, fair wear and tear so that the policy, without extension is old for old, or

indemnity and reinstatement is in addition and B3 is loss or damage directly or indirectly caused by earthquake. So earthquake is excluded, brought back in by an extension and then we get to C. And it sets out the amounts you can claim and it is the amount of loss or damage or the estimated cost of restoring. It is not a sum of money.

WILLIAM YOUNG J:
I am sorry, where does the insurer have the right to do the repairs?

MR GRAY QC:
They don't Your Honour. There is no express provision saying that.

WILLIAM YOUNG J:
Well that is the point I was making and on the face of it, they had to pay out after the first event, the amount of the loss or damage or the estimated cost of repairs. If they had done this, this argument wouldn't arise.

MR GRAY QC:
I accept that Your Honour.

WILLIAM YOUNG J:
So are they entitled to change the dynamic of the policy by insisting on a course of action over the protest of the insured. Would you say they had a right?

MR GRAY QC:
In my submission, yes that what the document merger is about.

GLAZEBROOK J:
Can I just check. Why do you accept, on your argument, that you wouldn't have to pay that money back?

MR GRAY QC:

Because if there is a claim – when there is a earthquake, when there is loss of or damage to the building, there is an immediate entitlement to be compensated for it. And if the underwriter had said, look it's too hard to get repairs done at the moment, I can't get builders, I can't get electricians, I can't get plumbers. I will pay you money instead, that would have brought that claim to an end.

WILLIAM YOUNG J:
So that's a complete reset.

MR GRAY QC:
At that – yes. It would have.

GLAZEBROOK J:
Also, so if the insurer in this case, it is probably just taking out the point that Justice Young just made to you, wrongfully, didn't do that, why should that change the position and why would it change the position in the marine situation. You say in the marine situation, if they had paid it out while they were at sea, then the marine merger doctrine wouldn't apply.

MR GRAY QC:
Right, let's take Your Honour's questions one step at a time. Your first question was if the underwriter had wrongfully not paid, there is no suggestion in this case that the underwriter has wrongfully not paid and in our synopsis we set out some core facts about this case because this case is part of a matrix of cases which are on their way through the Courts and some of which will arrive here. And this has its own narrow set of facts and problems but in none of them is there any criticism of underwriters for not affecting repairs and not paying.

WILLIAM YOUNG J:
I think there is criticism here for not paying.

MR GRAY QC:

Well I don't accept there is an obligation to pay.

WILLIAM YOUNG J:
I think there is a suggestion that basically they should have paid out and they didn't have an entitlement to do the repairs themselves.

MR GRAY QC:
With respect, hasn't been made before and I don't understand –

WILLIAM YOUNG J:
Well I am pretty sure it has been made before actually. I don't think I came up with it myself.

GLAZEBROOK J:
But isn't that the letter that we were taken to where they said, please pay out at page –

MR GRAY QC:
Your Honours we are going all round the place. Can I try and get some order to this and explain where I would like to take these submissions. The limited fact is there is no criticism for non payment. The payment contemplated by the policy is the cost of repairs and repairs could not be undertaken. And the repairs could not be undertaken for very good reason.

GLAZEBROOK J:
Can you just repeat that, I think I missed what you said at the beginning.

MR GRAY QC:
The repairs were not undertaken.

GLAZEBROOK J:
No, no I got that. You said the indemnity was for the cost of repairs?

MR GRAY QC:

Yes. Even if we – we will come in time to the argument that came around in the Court of Appeal for the first time. Well gosh if we haven't got an entitlement to be indemnified for the cost of repairing our building, we have got a right to receive a sum of money and this is actually a policy which is a promise to just pay a sum of money without repairs being undertaken. A different proposition, you will note, from the one that says, "If my whole house burns down, I can get the value of my house and not rebuild the house." That's a different proposition, in the cases you were taken to, in that regard were different cases. Though if we look at the first line of C1, "This insurance will pay the amount of loss or damage or the estimated cost of restoring." It is about what is the damage, how much does it cost to repair it, and then getting that, subject, of course, to in the case of C1 to an adjustment for betterment because the repairs would be new for old. But that's an adjustment that gets made in all sorts of cases. And the similarity between these facts and the marine cases, is that in marine cases sometimes for good reason, repairs are not undertaken immediately and that is because the vessel is at sea and there can't be. And that is the factual similarity between the marine cases and this unique New Zealand fact situation, which makes the doctrine of merger appropriate. It is that the repairs could not, for good reason, be undertaken and so at the expiry of the policy when the building had been destroyed, no loss had been suffered by reason of the prior repairs because the whole building had been destroyed.

WILLIAM YOUNG J:

You're treating the policy as a policy where your primary obligation is to repair the building. And that got frustrated because, to use a non-technical word, because of the sequence of events and the final damage to the foundations or whatever.

MR GRAY QC:

For a good reason.

WILLIAM YOUNG J:

As opposed to treating it as a requirement of the policy to pay out money.

MR GRAY QC:

All insurance indemnifies for loss. I mean our synopsis and our bundle begin with general insurance cases saying the very core of insurance is to indemnify for loss, not more, not less, begs the question, of course, what is indemnity?

WILLIAM YOUNG J:

Yes but sorry. Para 1, C1 is presumably to pay either the diminution in value as a result of the accident, that's the amount of loss or damage or (b) its estimated cost of repair on a like to like basis.

MR GRAY QC:

Of restore, estimated cost of restoring.

WILLIAM YOUNG J:

But if they are just policies to pay money, they are not policies for you to take over the project, run it yourself, in conjunction with obviously lots of others.

MR GRAY QC:

No it is silent on that, and because it is silent, the insured as the owner would be the party that would be doing the repairs.

WILLIAM YOUNG J:

Or just taking the money, it doesn't have to repair.

MR GRAY QC:

I don't know if that is so in relation to damage.

WILLIAM YOUNG J:

Look I am not sure, I am just thinking of the case that Mr Carruthers cited. I would have thought that under C1, if you had paid out the insured $197,500 as requested, they wouldn't have been under an obligation to repair would they?

GLAZEBROOK J:

And they have decided to buy a new asset, mightn't they. They might have said that this asset was old. Say they didn't have a replacement cost, they might have said this asset is old, it is now obsolete effectively and I don't want it repaired. I want to get a new one and I will take my 190,000 or whatever it is, and add my other 300,000 and buy a new one.

MR GRAY QC:

Or I will have a holiday or do anything.

GLAZEBROOK J:

Well do you accept that they can do that?

MR GRAY QC:

No.

GLAZEBROOK J:

Well what do you say they have to do, that they have to say, "Oh I don't care; it doesn't matter if this is an obsolete asset, I can't use that money for something else."

MR GRAY QC:

Well Your Honour asked the question of my learned friend about obsolete assets. There are obsolete asset cases where the replacement –

GLAZEBROOK J:

Obsolete is probably the wrong word in those circumstances. It is just one that they decide they want a new one, rather than repair the old one and you are saying they can't do that.

MR GRAY QC:

We say that C1 is about repairing and the reason for that is this. Supposing it is a $1000 building and it has $20 worth of damage and the insured wants to

take the $20, not repair but then argue that its building remains worth $1000 if there should be another accident.

WILLIAM YOUNG J:

Can you actually point to any authority that says that an insured, who is compensated for diminution in value, or for estimated cost of restoration, has to spend the money on repairing the asset as opposed to, for instance, selling it in its diminished state.

MR GRAY QC:

No I haven't turned up ready to do that to Your Honour and of course in the way Your Honour phrased the question which is compensated for diminished value or repairs, some of the answer already is incorporated in the question itself.

WILLIAM YOUNG J:

Well is it? I mean you have perhaps gone off in a bit of a tangent but if it is a serious argument I would like to know. If it is an argument seriously advanced I would like to know some authority which supports it because on the face of it, the case that Mr Carruthers took us to, do suggest that the insured doesn't have to do any such thing.

MR CARRUTHERS QC:

The point I was trying to make at the beginning was we differ from our learned friends in the significance of marine cases and the essential characteristics of marine cases which they say make marine cases inapplicable here and in particular we say that it is not true, in marine insurance that the right to make a claim is deferred until the end of a voyage or that the notion of a marine adventure determines the nature of marine insurance.

TIPPING J:

How do you deal with Lord Birkenhead's cryptic comment that if the right has accrued, you'll remember that passage was –

MR GRAY QC:

Yes, I –

TIPPING J:

– such and such. If it hasn't accrued, such and such else, because that seems to turn on whether or not the insured is under – insurer is under a liability. If the liability is postponed till the end of the voyage then presumably it hasn't accrued, but you're saying that the liability actually accrues at the time of the event causing the harm to the ship but you don't actually quantify the loss until the end of the voyage I think is the distinction. You didn't put it quite like that but I understood that to be the distinction you were –

MR GRAY QC:

That's where the repairs –

TIPPING J:

– making, is that right?

MR GRAY QC:

Yes, where the repairs are not undertaken.

TIPPING J:

But the liability has accrued, the repairs are not undertaken, so quantification of loss does not occur until the end of the voyage. Is that what you're saying?

MR GRAY QC:

Yes, Your Honour. The limitation period starts to run –

TIPPING J:

Yes.

MR GRAY QC:

– immediately on the event. The limitation period is not deferred to the end of the voyage. The limitation period starts and if the repairs are undertaken the

liability to pay for the repairs arises immediately. It accrues. It's where the repairs are not undertaken that the loss which is the diminution in value, as Justice Tipping says, isn't quantified to the end of the voyage and the liability to pay doesn't arise until then.

TIPPING J:
Well, this –

MR GRAY QC:
And I will take Your Honour through those passages.

TIPPING J:
Yes, well, I think this is the key to it myself. This is – never mind the precise wording of C1 and 2 and so on. I think this is the key point in the case. If there is a good case for extending the marine insurance approach into this field, you're making progress. If there isn't, you're not making progress.

MR GRAY QC:
Yes, I understand that, and, to be honest, the primary argument made by the underwriter in all Courts was that actually merger is the explanation for this and our analysis of the Court of Appeal judgment is that the finding is merger in all but name, when we come to it, because in the key paragraphs of what the Court of Appeal said it is there were no repairs as a result of the – well, there were some repairs after the first and second earthquakes. They were paid for. Other repairs were not undertaken. There were no repairs after the third earthquake. There can be no claim for repairs which were not undertaken under C1.

TIPPING J:
Well, if limitation doesn't – runs at the time of the damage to the ship, the unrepaired damage to the ship, then in accordance with the terminology of limitation law the cause of action must accrue –

MR GRAY QC:

Yes.

TIPPING J:

– at the time of the damage, unrepaired damage to the ship.

MR GRAY QC:

I will come to take Your Honour to that authority, but there's also *Kastor Navigation Co Ltd & Anor v AGF MAT (The Kastor Too)* [2004] EWCA Civ 277; [2004] 2 Lloyd's Rep 119 which I will take you to, which is a case where there was damage, the cost of which, the cost of the repairs for which, would exceed the value of the vessel so that within the notion of constructive total loss in marine insurance there was a constructive total loss and then shortly after there was an actual loss. The underwriter said, "I'm not liable for the constructive actual loss because there's a total loss within the period of the policy, and that's a supervening event and the losses merge," and the Court said, "No. When there is a constructive total loss, the right to recover arises immediately and you have to pay." And –

McGRATH J:

All right, now, we've been peppering you a bit, Mr Gray.

MR GRAY QC:

Well, that's always the pleasure of being here.

McGRATH J:

Just one of the pleasures fine but just as long as you're getting your argument to us. So perhaps we should give you just a little chance to proceed a bit further on your own.

MR GRAY QC:

Your Honours, let's go through the authorities and read them in detail and then see where that gets us to. We start in the bundle of authorities at page 1 with *Castellain v Preston*, not an insurance case. I won't take Your Honour

through it, but it is for the proposition that the whole point of insurance is to indemnity for loss.

The first case then is *Livie v Janson*. That's found at 15. I've extracted the passage from the judgment of Lord Ellenborough, Your Honours. It's found at pages 20, 21 and 22 of the case book. The question is posed on page 20 in the third paragraph, "This was an action on a policy on a ship and goods, warranted free from American condemnation. The ship and goods were seized by the perils of the" – "were damaged by the perils of the seas, and were afterwards seized by the American Government and condemned, and the question is whether the total loss by subsequent seizure and condemnation takes away from the assured the right to recover in respect to the previous partial loss by sea damage. In consideration, we think it does," and the analysis then continues over page 21 on about line 8, "Considering the deterioration of the ship and cargo then as the extent of what is referable to the head of sea damage, we think we may lay it down as a rule that where the property deteriorated is afterwards totally lost to the assured, and the previous deterioration becomes ultimately a matter of perfect indifference to his interests, he cannot make it the ground of a claim upon the underwriters. The object of a policy is indemnify to the assured, and he can have no claim to indemnity where there is ultimately no damage to him from any peril insured against. If the property, whether damaged or undamaged, would have been equally taken away from him, and the whole loss would have fallen upon him had the property been for ever been so entire, how can he be said to have been injured by its having been antecedently damaged? To put another instance to the same effect, supposing ship and cargo to be damaged in the early part of a voyage by the ordinary sea perils, and afterwards wholly destroyed by fire before the voyage is finished, of what consequence to the owner is the damage which may have occurred from one or several successive causes of injury before the fire? And if the property, whether damaged or not, would have been equally annihilated, is not its previous deterioration wholly immaterial?"

GLAZEBROOK J:

Do you have the terms of the policy at all?

MR GRAY QC:
This policy?

GLAZEBROOK J:
Yes.

MR GRAY QC:
No. The interesting facts of this case is that the damage was caused by an insured peril and the loss was not. So –

WILLIAM YOUNG J:
Well, it was warranted free of American condemnation so it was –

MR GRAY QC:
And it was seized by the Americans and condemned.

WILLIAM YOUNG J:
But in a way it's sort of slightly circular because in this case the question is what are the losses for which the insured are entitled to indemnity, because here, here there's in the end only one loss because there's one product, one item. It's a value policy. They can only lose what –

MR GRAY QC:
It's not with a value policy, with respect, Your Honour.

WILLIAM YOUNG J:
I think it was, wasn't it?

MR GRAY QC:
It's subject to a limit but it's not a value policy.

WILLIAM YOUNG J:

Sorry, which – I thought this one was a value policy.

MR GRAY QC:

No, no, with respect, Your Honour, it's a limit, not a value. The policy is page 74, Your Honour.

WILLIAM YOUNG J:

No, no.

GLAZEBROOK J:

No, no, in this case.

WILLIAM YOUNG J:

In this –

MR GRAY QC:

I'm sorry. Yes, I'm sorry, yes.

WILLIAM YOUNG J:

The case you were – that was a value policy. Whereas here, the damage that was done in September got worse. There was more damage done in December and more damage done in February so it was a – there were losses which the insured kept on suffering from or continued to suffer on each event.

MR GRAY QC:

Yes, and the problem was the property's under insured.

WILLIAM YOUNG J:

Well, you – well, that's the whole question of the case, isn't it?

MR GRAY QC:

Well, it's a factual question.

WILLIAM YOUNG J:

Well, it's not what – it's a limit.

MR GRAY QC:

Suppose the building had been worth the limit, then we wouldn't be here, because –

WILLIAM YOUNG J:

Possibly not. It would be – yes.

MR GRAY QC:

– at the time of the fourth event the value of the building would have been the limit less the cost of the prior damage.

WILLIAM YOUNG J:

Yes, that's true. Yes, I agree.

MR GRAY QC:

So we wouldn't be here. So what you're being asked to do is to protect against the consequences of under-insurance.

WILLIAM YOUNG J:

But it's a loaded expression. All he's done – all they've done is set a limit on insurance and they may have said, well, we don't think we'll lose the lot in one go.

MR GRAY QC:

Well, then we're in the Fire Service cases, aren't we, with the policies that underlie the practice of insuring in that way?

WILLIAM YOUNG J:

But is there – this isn't a – they're not saying this is the value, average doesn't apply.

MR GRAY QC:

Correct. This is a policy with a limit.

WILLIAM YOUNG J:

So are there cases about policies with limits that…

MR GRAY QC:

No, I'm not aware of any, Your Honour.

McGRATH J:

So that's *Livie v Janson*?

MR GRAY QC:

Yes. The next case is *Lidgett v Secretan*. A factual distinction in *Lidgett v Secretan* was that the damage occurred in the course of one policy and the loss occurred in the course of another. At the end of the first policy, repairs had commenced but not been finished and the vessel had a diminished value by reason of the uncompleted repairs. It was the same underwriter and the underwriter offered to pay in respect of the second policy the diminished value of the vessel and in respect of the first policy, the amount of the repairs undertaken but not to pay the difference between the value of the repairs undertaken and the diminution in the value of the vessel. And the case says that is what you do have to pay, because the loss that is suffered which comes to a head at the expiry of the period of the insurance, where repairs have been commenced but not completed, is the diminished value of the vessel.

GLAZEBROOK J:

And do you say that's the case here under this policy or is it because – let's assume there is only one earthquake and at the end of the time, there's no repairs having been undertaken and that's the end of the insurance. What do you say has to be paid out under this policy?

MR GRAY QC:

Ordinarily what would occur in those circumstances is the underwriter would agree to pay the cost of the repairs and there would be a performance of the contract.

GLAZEBROOK J:
Well they might agree to do that. Can they be required to do so because I would have thought they probably can?

MR GRAY QC:
Yes Your Honour they have to behave reasonably, and they have to get on with it and not unreasonably delay although the insurance code is not binding, I have no doubt that it will have some force.

GLAZEBROOK J:
Well I was actually asking under the policy.

MR GRAY QC:
It would require an implied term Your Honour.

GLAZEBROOK J:
Well it is just that that is a distinction from the cases you are discussing in the marine situation isn't it?

MR GRAY QC:
In my submission Your Honour, the circumstance here is that like the marine cases, for good reason these repairs were not undertaken, they couldn't be. No one was deliberately delaying. Everyone was doing as well as they could in very, very difficult circumstances. In oral argument in the Court of Appeal the learned president asked the question, "What happens if there is damage in one policy period and destruction in a different policy.?" And *Lidgett v Secretan* was the answer but that was the topic of concern to His Honour in oral argument and may or may not be a factor which contributed to the judgement of the Court of Appeal being expressed in the way that it is, which is focussing on –

McGRATH J:

Because of concern in relation to the Christchurch situation as I recall.

MR GRAY QC:

Yes.

GLAZEBROOK J:

And so I am sorry, that concern was expressed – do you want to just take us to what you are saying was found by the Court of Appeal that might have been influenced by that so I can understand the point.

MR GRAY QC:

Well we say the decision of the Court of Appeal is to be found in paragraphs 48 and following on page 25 of the case. By this stage the Court of Appeal has decided that the argument made in the pleadings and the arguments made by the appellant were in fact, four C2 claims. At 49 they say, in claims relating to damage but not repairable building, the respondent is liable under clause C2(a)(i) in respect of each happening for the cost of restoration, the quantification of the liability depends on the repairs actually being made and the liability equates to the actual cost of those repairs. In the present case the cost of the repairs actually completed as payable, in addition the cost of repairs actually completed after the second is payable. That so despite neither being fully repaired." In relation to third, and they record the different positions of the parties but then go on 51 to say, "On the view taken by Ridgecrest that the building remained repairable after the third earthquake, the liability in respect of the claim arising from the third earthquake would be zero because no repairs have been undertaken and therefore no costs of repairs have been incurred by Ridgecrest for which a claim could be made."

WILLIAM YOUNG J:

This all proceeds on the basis that we can put a blue pencil through C1 doesn't it?

MR GRAY QC:

Yes it does but my submission is that 51 is merger in all but name and in fact what the Court of Appeal has found is merger, they just haven't wanted to call it that. They have said they are under C2, they have said there is a liability under C2 to pay the cost of repairs but they've said because no repairs were undertaken, there can be no claim.

BLANCHARD J:

But that is on the basis that they think that they are looking at a claim for replacement not an indemnity claim.

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

Well couldn't you say, all right there are already three claims here, September, there are four claims, probably five actually? September, December, they are indemnity claims; February, maybe indemnity, maybe restoration; June, restoration. So why can you lock into a single repair claim, what are discreet events? Because your argument is much better if the obligation of IAG is simply to repair the building.

MR GRAY QC:

It is reinstatement is the final claim, restoration is another word that is found in C1 so that the semantic differences are unhelpful. The semantics are unhelpful.

WILLIAM YOUNG J:

Sorry. What I am trying to draw a distinction on is between indemnity claims under C1 and a restoration or a reinstatement claim under C2. So you could face two indemnity claims plus a reinstatement claim.

MR GRAY QC:

At the insured's election.

WILLIAM YOUNG J:

But you want to just apply a single cap.

MR GRAY QC:

I want to say, no matter which, what is the loss suffered, the loss suffered is the destruction of the building. All of the damage which occurred, before the destruction of the building was of no moment to the insured and if merged in the total destruction and the entitlement of the insured was to be indemnified in terms of the policy on the total destruction of the building, and it has been.

GLAZEBROOK J:

What I cannot understand on that argument, again, is why if it has already been paid out, does that destroy that argument because in fact that will be the same case, whether it has been paid out or not. So if it has been paid out and repairs haven't been undertaken, then the only loss that has been suffered is the destruction of the building.

MR GRAY QC:

I am sorry I am not quite understanding your question, which is probably why I haven't answered it.

GLAZEBROOK J:

I understood you to say that if after the first earthquake, there had been a payment out of the estimated cost of repairs, and then another earthquake had happened immediately afterwards, that there would be a reinstatement cost and the total loss of the repairs or the estimated cost that hadn't occurred and the total loss of the building and yet in both cases just because the insurance company might have paid out or not paid out, is that the only losses and the total destruction. So I cannot understand why and then, of course you will get into the issue of whether they rightfully paid out because I was looking at page 100 where there was the letter saying, "Pay us out."

BLANCHARD J:

Presumably because that is merger cannot take place if there has been an adjustment.

GLAZEBROOK J:
It just does not make any sense.

BLANCHARD J:
And the payment out on that hypothetical constitutes an adjustment or settlement.

GLAZEBROOK J:
So if it should have been settled –

TIPPING J:
There is no loss left to merge if it has been paid out.

MR GRAY QC:
The policy has responded.

WILLIAM YOUNG J:
To put it another way, to use the language used before. There is undoubtedly a complete reset, you start from scratch there is still the 1.98M cap and that is unaffected.

MR GRAY QC:
Well there is one point but there is cover for any future event and liability is limited to 1.98 which is Your Honour's cap.

WILLIAM YOUNG J:
For any single happen.

MR GRAY QC:
Yes. The property, if unrepaired, might no longer be worth 1.98. But that's a factual that we don't get to in this case. But in normal circumstances, if there

was adequate insurance and the property was worth 1.98 and there was half a million dollars worth of damage caused but not repaired, the market price for the building would reflect the unrepaired damage and that is the way the insurance would work. So that there would not be windfall in those circumstances.

WILLIAM YOUNG J:
But it's only a windfall here if setting a limit lower than the value of the building is under-insurance. Is treated as under, as seen as morally under-insurance.

MR GRAY QC:
Well the traditional position is that where there is under-insurance the insured is regarded as being their own insurer for the balance and so morally if we ask where should the cost of insuring that part of the value of the building lie, it should like on the party that's regarded on being their own insurer.

WILLIAM YOUNG J:
Well it is conclusory because if you look at the other way then they were probably well enough insured. The policy bears the meaning that Mr Carruthers contends for.

MR GRAY QC:
Yes, this is not a unique position –

WILLIAM YOUNG J:
No, it's not.

MR GRAY QC:
– where people don't have sufficient cover and are looking to address the inadequacy of –

WILLIAM YOUNG J:
Some of them will be –

BLANCHARD J:

The argument could still be being made if the property had been fully insured, as I understand Mr Carruthers argument.

GLAZEBROOK J:

Yes.

BLANCHARD J:

So really the under-insurance is a red herring.

MR GRAY QC:

Your Honour, if the building was fully insured, and payment was made for the unrepaired damage, the market value of the building at the time it was destroyed would be diminished.

GLAZEBROOK J:

But isn't it –

BLANCHARD J:

But the cost of replacement wouldn't be affected.

MR GRAY QC:

Well –

BLANCHARD J:

You've got a hybrid policy here.

MR GRAY QC:

On a C1 it would because it's to the condition –

BLANCHARD J:

On, yes, but if –

GLAZEBROOK J:

But on a C1, on a C1 you don't need merger.

BLANCHARD J:

If it's C2 it's simply a replacement cost which –

WILLIAM YOUNG J:

Might depend on the details mightn't it because you'd be obliged to reinstate a building that's not in great order. Now whether that has got any – is material or not may just depend on what bits are damaged.

BLANCHARD J:

Well in this sort of scenario the building is going to be pulled down and there's going to be a replacement building, either on this site or a different site.

GLAZEBROOK J:

But you don't need merger on a C1 argument, do you, because in fact you would be, if you did have merger you would actually be selling the insurance short wouldn't you? Because one assumes that if you've got an unrepaired building there'll be a diminution in market value so you will actually have lost the initial damage whether it's repaired or not and the value of the building at the end. So the insurance company's argument there would actually sell the insurance short, wouldn't it?

MR GRAY QC:

We say no, Your Honours, because we've paid the limit of the value of the policy so we have treated as being wholly destroyed in the final event. No deduction has been made for diminution in value by reason of prior damage. The whole of the limit of value has been paid following the fourth earthquake, or the third.

TIPPING J:

The limit sets the cap, obviously, and previous damage is really irrelevant.

MR GRAY QC:

Yes. It's treated as –

TIPPING J:
That's already liable for that fourth earthquake.

MR GRAY QC:
Yes.

TIPPING J:
The problem arises that you appear under the literal terms of the policy to have had accrued against you three separate claims. That's your problem, isn't it, and this is why you have to be able to show that those losses, if you like, are no longer valid losses or have gone away somehow.

MR GRAY QC:
Well the law regards them as merging –

TIPPING J:
Exactly.

MR GRAY QC:
– in the total destruction.

BLANCHARD J:
You're trying to merge the indemnity portion of the policy into the replacement cost of part of the policy. You have a hybrid policy and you're trying to merge the two parts of it aren't you?

MR GRAY QC:
Am I trying to merge the indemnity? I am trying to construe the policy as a whole so I say that each part is informed by the policy as a whole. And I am facing arguments which slip between C1 and C2.

BLANCHARD J:
Yes.

MR GRAY QC:

As and then but the answer is yes the limit, which is expressed as a C2 limit, is regarded by the policy as being a C1 limit as well and has been paid.

WILLIAM YOUNG J:

Say in the – that there was a complete breakdown in relationships over Hawkins Construction in late 2010 and the insured had issued proceedings, it probably, you know, time constraints permitting, probably would have got summary judgment for 197,500 which – because that was actually less than the estimated costs of repair. What answer could there have been to a claim for a figure that was less than the – any reasonable –

MR GRAY QC:

There are so many factors – I understand the force of what Your Honour is saying. Whether the answer to that is just an unqualified "yes", I'm not certain. There are…

WILLIAM YOUNG J:

Well, if it were an unqualified "yes", you would have to be able to say that subsequent events, as it were, erase that cause of action.

MR GRAY QC:

I say the loss which would have been the basis for that cause of action merges in the total destruction of the building and that the indemnity available under the policy is the limit of cover consequent upon total destruction, and I say that's what the law is. I say that –

TIPPING J:

But if due to the vagaries of time, or putting it the other way round, if things were to work very swiftly, as one would hope they could but it's quite unrealistic, you'd actually have three judgments against you, wouldn't you, for the estimated cost of each of the three, the first three earthquakes, before you get to the question of the loss on the fourth earthquake.

MR GRAY QC:
Depending on what the estimated cost is…

TIPPING J:
Yes, this is the point that worries me. It shouldn't really depend on the accidents of time, should it? If there is actually an accrued cause of action on each of the first three earthquakes on which you're entitled, or the plaintiff's entitled –

MR GRAY QC:
Yes.

TIPPING J:
– to a judgment, why does the fourth earthquake take away those entitlements and substitute with only just that one entitlement?

MR GRAY QC:
The law has asked itself that question and the answer in the authorities is because to do that is to over-compensate and it is not an object of contracts of insurance or the law of insurance to give an insured more than the value of the property wholly insured, and therefore those –

TIPPING J:
Well, that may be the –

MR GRAY QC:
– earlier causes –

TIPPING J:
– general rule but if the policy is so constructed as to contractually give that right, it can only be done through the concept of a loss that has already accrued being overtaken.

MR GRAY QC:
As it has been in this case factually.

TIPPING J:
Well, this is where I think you've got work to do, Mr Gray, but what I would be particularly interested in is any authorities anywhere, whether in America or wherever, that say that outside the marine environment, where clearly a rule seems to have emerged from mists of time, you apply this rigorously, never mind the precise terms of the policy.

MR GRAY QC:
Yes, no, we've looked for those and can't find them.

TIPPING J:
Right-o.

BLANCHARD J:
Have you looked in the United States?

MR GRAY QC:
Yes, one can always look further in the United States.

BLANCHARD J:
Well, I'm not familiar with insurance law at all really so I don't know what leading texts in America there are on insurance.

MR GRAY QC:
I have checked texts but not gone beyond that. Can I say this, my learned friend tells me he's looked and also hasn't found anything. When Your Honour says "emerged from the mists of time", originally there was only marine insurance.

TIPPING J:
Yes.

MR GRAY QC:

Insurance law was marine insurance law. Then later there was life and then fire and then material damage in the second half of the nineteenth century when insurance companies were able to be formed. Lloyds itself didn't open to material damage policies until the last quarter of the nineteenth century, and those policies took marine insurance. So fundamental tenets of insurance law were determined in the context of marine insurance law, and this doctrine of merger was not created specifically within marine as a subset of insurance.

TIPPING J:

I can understand the marine. It's usually a single voyage. Here we have by contract a perpetually renewable cover within the same claims year subject to each event having its own limit. So you have in a sense four contractual rights accruing on the happening of the four earthquakes. Would you go as far as that with me, leaving aside the question of how you quantify the loss?

MR GRAY QC:

There are either three or four events, depending –

TIPPING J:

Yes, yes.

MR GRAY QC:

– on when the building was destroyed. Yes, I accept that there were events.

TIPPING J:

So the only escape, if you like, from your client's point of view, is through some approach to the quantification of the loss on the happening of the fourth event.

MR GRAY QC:

Yes. In agreeing with Your Honour can I say this? If there had been four events and if each event had caused loss short of destruction, there would be a liability to pay for the cost of repairs for each of the four events –

TIPPING J:
And if each –

MR GRAY QC:
– and they would accrue at the time of the event. That's – I mean, I can't avoid that.

TIPPING J:
No. So if each – theoretically, if each of the four events was half a million, two million in total, you'd have to pay that because it's cap per event?

MR GRAY QC:
You can pay more than the limit –

TIPPING J:
Yes.

MR GRAY QC:
– in the course of a policy period, yes.

TIPPING J:
The policy is constructed, so it seems to me, subject to your assistance, on the basis that each event is a self-contained issue, both as to liability and as to quantum.

MR GRAY QC:
Yes, but we say we're being asked to pay for the same loss more than once. We – the answer to Your Honour's line of questions, and forgive me if I'm jumping ahead, is to say –

TIPPING J:

No, no. I'm –

MR GRAY QC:

That's fine. Yes, all of that's fine, but by paying for the whole of the building at the end we're paying for the broken windows, for the damaged roof, for the wall that's been knocked over, more than once and that's never contemplated.

TIPPING J:

Is that a better way of putting it than saying that the earlier loss merges in the later? Is it a better way of putting it is just what you've said? You're being asked to pay for the loss that has accrued on the first, second and third occasions a second time by dint of the fourth claim?

MR GRAY QC:

That's what – that's the reasoning in the case. The reason for the merger rule is that you are being asked to pay for the same loss more than once and you are paying more than the insured could have received for the complete destruction of the insured property.

WILLIAM YOUNG J:

How – if you had sought to capture all this in a clause that could have been put in the policy, would it have been something along these lines, that in respect of any one policy year the maximum liability of the insurer in respect of unrepaired damage is the capped amount no matter how many happenings have contributed to that damage? Because some – all the arguments you're advancing do seem to me to come back to a proposition along the lines that the cap can apply to all losses in a single year, that it's not quite a total maximum because you could have broken events that are settled one by one, but if it's unrepaired at the end of the year it all goes into the pot.

MR GRAY QC:

For good reason, Your Honour. Where for good reason repairs have not been able to be completed when the building is totally destroyed you only paid the limit of the liability for the building.

GLAZEBROOK J:
So let me get this straight. The rule only applies where you've got a total destruction.

MR GRAY QC:
In the same policy period.

GLAZEBROOK J:
In the same policy period. Otherwise what you could have – well, there's probably a number of things I want some assistance on but – because the – the whole idea of where for good reason repairs haven't been able to be done assumes that you have to do repairs, which I don't think emerges out of this particular policy. So perhaps start with that. Why do you have to do repairs?

MR GRAY QC:
Because the indemnity in C1 is to have repairs undertaken, to be indemnified for loss of – that the operative clause is, you are insured for loss of or damage to. Loss of is destruction, damage to is damage short of destruction.

WILLIAM YOUNG J:
That could simply just be diminution of value.

MR GRAY QC:
The damage to could be diminution of value. C1 is only the quantification, it is not the operative clause. C determines the amount, not the nature of the cover. The cover is found in the page earlier in the operative clause.

GLAZEBROOK J:

Yes but loss of. Well let's just look at that then. "Loss of" means the whole thing has gone. "Damage to" means there is damage. Well there has been damage, if somebody goes into the back of my car there has been damage.

MR GRAY QC:
Right, if you elect not to repair it, then as His Honour Justice Young said, that the quantum of loss is the diminished value.

GLAZEBROOK J:
And where do you get that from – clause?

MR GRAY QC:
No, I don't get that from the clause. It is not what the clause says, but if you look at –

GLAZEBROOK J:
Well we are just looking at an insurance clause. So in C1 where do I get that "Or pay the amount of loss or damage or the estimated cost of restoring."

MR GRAY QC:
Well we pay the amount of loss of, that's the link back to the limit.

GLAZEBROOK J:
Well no it is not, it just says, "loss" and then it will be subject to a limit.

WILLIAM YOUNG J:
This is the operative clause isn't it. This means the insurer will pay, that's the key promise isn't it?

BLANCHARD J:
This clause is not helped by having some prepositions missing from it. It is presumably supposed to read, "The amount of loss of or damage to."

MR GRAY QC:

The insured property.

BLANCHARD J:
Your business assets.

MR GRAY QC:
Yes. "And quite what estimated cost of restoring your business assets to the same condition." That contemplates that they have been restored or will be restored.

WILLIAM YOUNG J:
No it just contemplates their estimated costs doesn't it. I mean that is likely, nothing is ever symmetrical in life, but that is likely to be equivalent to the diminution in their value.

MR GRAY QC:
Yes but may not be in some cases. And what happens if the person does it themselves. They don't recover because it is costs not value of work.

TIPPING J:
Your argument presumably is that if one focuses on the word "restoring" and there has been no restoration before the total loss, a la *Wright Stephenson*, the total loss can never be restored, sorry the restoration contemplated by one can never be undertaken, therefore you limit yourself to the limit for the final event.

BLANCHARD J:
Or the diminution in value caused by the first event etc.

TIPPING J:
Yes.

MR GRAY QC:

I say that the cost of restoring contemplates restoration. It is not money in lieu of a restoration which never takes place.

TIPPING J:

Personally I am not too hung up on this awkward grammar or the precise words of C1 and C2. What I would like to know is, what authority is there to suggest that in a situation of marine insurance, you could end up having to pay twice, if you like. Mr Carruthers made a significant point about how you don't quantify until the end of the voyage.

MR GRAY QC:

Yes and we say that is wrong.

TIPPING J:

Well for myself, I would have thought that's where we all should be looking.

MR GRAY QC:

Right. We had arrived for our most excursion at *Lidgett v Secretan* in the judgment of Willies J. That begins at page 24 on the volume . His Honour's judgment begins at 27 and he sets out the facts. "The case involves two questions. It appears the vessel was insured by one policy on the voyage from London to Calcutta and for 30 days after her arrival there in safety, and also by another distinct policy on a voyage from Calcutta to London. She appears to have sustained damage by striking on a reef on her voyage out; and in respect of that damage there was a partial loss under the first policy. It also appears that, after the expiration of the period for which she was insured by the first policy, and after the second policy had attached, and after the repairs rendered necessary by the accident which occurred on the voyage had been partly done, but before they had been completed and the damage which the ship had sustained had been entirely made good, she was totally destroyed by fire. She arrived in a damaged state at Calcutta worth less than she would have been if the damage had not occurred."

Now over at 624 at the left-hand, Your Honours.

WILLIAM YOUNG J:

Sorry, what page, sorry, 624?

MR GRAY QC:

Yes, 28 of the bundle. "Let's look at the first policy and see what are the rights of the plaintiffs under it. As to what was actually done in the way of repairs, no question arises, but the question is whether the underwriters on the first policy are liable for particular damage done to the vessel during the existence of that policy, the repairs of which were not actually completed when the ship was destroyed. That raises the question whether the assured can in any case recover from the underwriters in respect of damage sustained by the vessel before any actual expense for repairs has been incurred, or, in other words, whether the assured is bound to go through the operation of repairing the ship before he brings his action against the underwriters. If in this case the owners had completed the repairs, it would have availed them nothing, by reason of the subsequent destruction of the vessel."

And then at the bottom third of the page, "Let's look at little closer at the matter. The ship at the expiration of the risk covered by the first policy was certainly reduced in value. Her owners were worth less, say by £1000, than they would have been if she'd arrived in safety. They had entered into a contract with the underwriters, whereby the latter agreed to indemnify them from the damage done to the vessel during the voyage. Is it not a damage to a ship that she is reduced in value from £5000 to £1000? In such a case, if the owners were dealing with the underwriters who were disposed to settle upon such terms as soon as the loss was ascertained, the loss would at once (on the expiration of the policy) be settled at £1000, and the assured would in the ordinary course receive a check for that amount." And that's the debate that we've been having, Your Honours.

And then the question of whether merger can apply is addressed half way down page 625. "Could the underwriter set up the merger of the partial loss in a total loss occurring after the expiration of the policy? In such a case, the

authorities would be called for, and the reasoning upon which they are founded would be considered. The authorities, when looked at, will be found to amount to this. A partial loss is not paid for if there is a total loss of the vessel during the period covered by the policy, because, when the underwriter pays the total loss, he actually discharges all partial losses occurring during the voyage, except such as fall within the suing and labouring clause, which are apart form the sum insured."

The suing and labouring clause enables you to recover money that you've actually spent getting repairs done. So you get money actually spent but otherwise no.

"He never stipulated to pay more than the total loss, and, if he were to pay for a partial loss, and also the whole value of the vessel, he would be paying more than he undertook to indemnify the assured against. There is another case, viz, where, after the vessel has sustained damage, but not been repaired, and has subsequently, and during the currency of the policy, been total loss by a peril excepted out of the policy, and in respect of which the owner was his own insurer." And that was *Livie v Janson*, and he discusses *Livie v Janson* and over the page, in the second sentence, says, "It appears to me that the authorities and the reasoning upon this subject go together. The former show that the rule in question is limited to the happening of the total loss during the time covered the policy, and the reason of the thing applies to the same period. Are we, then, to extend the doctrine of merger to the case of total destruction of the vessel after the expiration of the policy?"

WILLIAM YOUNG J:
If you treat each event as separate so that the cap resets after each event, this case is against you, isn't it?

MR GRAY QC:
No, in my submission no, because of – because the manner on which the case is deciding is that the losses merge.

WILLIAM YOUNG J:

Well, in this case, I suppose the drive of the litigation was that the ship was a valued policy, so the value of the policy didn't necessarily reflect its diminished state when it arrived at Calcutta. So there was a sense in which the insured was, got a pretty good outcome from the litigation, a thousand pounds for the damage and then full value of the ship as recorded is its value.

MR GRAY QC:

In my submission that is not the case.

WILLIAM YOUNG J:

Isn't it?

MR GRAY QC:

The insured gets what the insured was entitled to which is the full value of the vessel, undamaged. In respect of the first policy it gets the cost of repairs and the diminution in value and in respect of the second policy, it gets the diminished value.

WILLIAM YOUNG J:

I thought here is the value policy.

TIPPING J:

They didn't get 6000 did they?

MR GRAY QC:

No.

TIPPING J:

They got 5000, not 6000, total.

MR GRAY QC:

Of the second policy, it is now only worth four.

WILLIAM YOUNG J:

But it was a valued policy wasn't it? I am not familiar with the case in the way that you are but I am looking at page 628.

MR GRAY QC:

628 Your Honour.

WILLIAM YOUNG J:

No that is a reference to another case but the Judge talks about –

GLAZEBROOK J:

It is 617 I think it is setting out the terms of the policy or the two policies.

TIPPING J:

But you couldn't, as against the second indemnifier, get more than the value of the ship in a damaged state surely.

MR GRAY QC:

Unless you had agreed with the underwriter that it had a damaged state.

TIPPING J:

Exactly.

WILLIAM YOUNG J:

The ship was valued for the return trip at £20,000. It had been valued, it was – I don't fully understand it. It seems to have been valued at £20,000 for the first policy but with an insurance cap of £18,000. And then the next, for the next policy it is –

MR GRAY QC:

10,000.

WILLIAM YOUNG J:

Was valued at £20,000 so that the valuation does not allow for any diminution but of course the market value of ships may have changed.

MR GRAY QC:

But they only had 10,000 worth of cover.

WILLIAM YOUNG J:

No, they were subscribed to £10,000.

GLAZEBROOK J:

And then underwritten. I am just not sure why you need merger in a clause that only gives you loss or damage. Because the fourth earthquake on this, the loss or damage would be the value of the repaired building but less the cost of repairing it to that value. And so on a C1 you don't need merger because the only thing the insurance company would pay out is that last loss.

MR GRAY QC:

You need merger.

GLAZEBROOK J:

Subject to being under insured you say?

MR GRAY QC:

Yes that is the answer. You need merger to deal with under-insurance, if there was adequate insurance.

GLAZEBROOK J:

So is that what the marine insurance cases are based on because I didn't think so. They were just based on the fact that you only got one lump sum in total.

MR GRAY QC:

They are based on yes, the understanding of what is the indemnity inherent in a policy of insurance. What is it that the insured is entitled to receive and the answer is, they are entitled to be indemnified for their loss. How can it be said that they have suffered the same loss more than once.

GLAZEBROOK J:
And the only answer when somebody has already paid out, is just that that is too bad because the insurance company has paid it out, you still then get more than your loss.

MR GRAY QC:
Yes.

GLAZEBROOK J:
It just doesn't make any sense to me.

MR GRAY QC:
I am sorry Your Honour you haven't because the property has been reinstated. It has returned to –

WILLIAM YOUNG J:
Well no it hasn't. Because that assumes that it has been repaired.

MR GRAY QC:
Oh well if a sum of money is paid in lieu of repairs, in settlement of an obligation to pay for repairs, then yes they get more.

WILLIAM YOUNG J:
On what I understand to be the insured's argument, they say they are entitled, if the building was repairable, up until June. So as of the 23rd of February they are entitled to payments of about two and a half million I think, on their theory of the case.

MR GRAY QC:

Yes.

WILLIAM YOUNG J:

And if their factual hypothesis is right, you would agree with that, to that point.

MR GRAY QC:

If the factual hypothesis is correct.

WILLIAM YOUNG J:

So if the building was repairable after the 22nd of February and there hadn't been any other events, and everything else is right, they get say two and half million, it's of that order I think.

MR GRAY QC:

Or repairs to that value.

WILLIAM YOUNG J:.

Yes. So the last earthquake actually took away accrued rights they had.

MR GRAY QC:

It becomes circular, Your Honour. My answer is the loss is merged.

WILLIAM YOUNG J:

Well they merged at a lower figure than what they had been earlier.

MR GRAY QC:

Insurance is about real property, it is about property and damage to property and indemnification for damage to property. It is not a wager, it is not about delivering money to people on the occurrence of events, that is gambling. It is about having a property which suffers damage and the cost of repairs for the damage are indemnified and if the building is destroyed, the value of the building is paid, in this case up to an agreed limit. That is what a contract of insurance does. It doesn't say, if you get three fours and an ace of clubs, we will pay you $10,000. Now by some accidents, that can happen but it doesn't

mean that is the core right of an insured under a policy of insurance. And what this analysis begins with that very core central question. What is an insured in a policy of insurance entitled to be indemnified for?

WILLIAM YOUNG J:
I am not quite sure how to capture this exactly in words. But you are treating the cap as though it was some sort of warranty of value, that no matter what, you will never get more than this for the structure of the building.

MR GRAY QC:
Well you fix the premium on the basis of that. You've charged for that amount of cover.

WILLIAM YOUNG J:
Well that is the conclusion you are contending for. It just doesn't tie in very happily or completely with each happening and I have actually struggled really to try and get a wording of how you might put this in plain English in a policy that made it clear to insured and insurer what the contention is. Or what the result is you are contending.

GLAZEBROOK J:
Well what you would say is, if the building is destroyed in the period of the insurance limit, you will not get paid for any amounts that have not been repaired due to any earlier events.

MR GRAY QC:
If the building is damaged but not repaired, and then destroyed, you only get the value of the destroyed value.

WILLIAM YOUNG J:
It would be very easy to say that wouldn't it.

MR GRAY QC:

It might have been thought to be unnecessary but how many contract cases end up in this Court, with the lawyers able to look back and say, gosh why didn't they say it this way.

GLAZEBROOK J:

But does it go without saying because if the building isn't destroyed, but you have successive happenings, you can get paid potentially. Say you had four happenings, you could get paid potentially $4 million whereas if on the fourth, it is destroyed, you get paid $1 million. So it doesn't go without saying in an implied term sort of sense, does it?

MR GRAY QC:

In my submission if you come back to the way in which the analysis is structured, it works. The underwriter is not saying we will never pay you more than $1.9 million. What it is saying is, is that at any one time you can't suffer more damage than $1.9 million and where there is damage which has been caused and not repaired, it merges in total destruction because the building can't be more destroyed than totally destroyed. And if you are asking us, in the case of total destruction, to pay for all the broken windows three times, then it is an over recovery, it is more than we bargained for and it is not required to indemnify you for the harm that you have suffered.

GLAZEBROOK J:

If you were totally insured, you would never be paying for the broken windows would you. So if the building – if you were insured for each happening for $4 million and the building was only worth $4 million, less the unrepaired amount, then you would never be doubling up would you. So you don't need merger. I suppose the point is do you need merger if you're totally insured?

MR GRAY QC:

No. If there was adequate insurance, no.

GLAZEBROOK J:

So it's a combination of total destruction and under-insurance?

MR GRAY QC:

Yes.

GLAZEBROOK J:

And where in the cases does it say that?

MR GRAY QC:

I suppose the answer to that, Your Honour, it comes back to the analysis that the construction of the policies and the development of the doctrine is centred on that analysis of what it is that an insured has suffered: what is their loss and what is the loss for which they can be indemnified?

GLAZEBROOK J:

How does it come down to that? How does the proposition that you have to have under-insurance as well as – sorry, I've forgotten what I said now.

MR GRAY QC:

Well, Your Honour, the –

GLAZEBROOK J:

As well as no repairs.

MR GRAY QC:

Yes. What the cases do say is that if you recover for the prior damage which is unrepaired and the total loss, you've received more than you've bargained for.

WILLIAM YOUNG J:

Not only that, you've received more than you've lost because these are cases where they are valued policies.

MR GRAY QC:

Yes. Your Honour, these – just staying with the authorities there to get through them, they do come together in *Wilson*, which is found in the bundle on page 33, and this was the different facts situation where the partial loss and the destruction occur within the same policy period but the partial loss is from an insured peril and the destruction is not, although the destruction is compensated by Admiralty. It's a wartime loss.

McGRATH J:
Yes.

MR GRAY QC:
And the question in the case is where the partial loss has not been repaired so the vessel has a diminished value, and the Admiralty says, "Well, we're only paying the diminished value," so that the ship owner, if they don't recover the diminished value, will suffer some real loss, what's the right way for the law to respond, and the outcome of the case is no, the losses merge, and the ship owner does not recover for the value of the repairs that have not been undertaken.

WILLIAM YOUNG J:
But it does give a reason for that –

MR GRAY QC:
Yes.

WILLIAM YOUNG J:
– which you will I suspect have to take us to and perhaps take issue with.

MR GRAY QC:
Lord Birkenhead is the judgment most often cited. It starts on page 35 in the bundle, 192 of the reports. His Lordship, the Lord Chancellor, sets out the facts. The respondents were the owners of the steamship *Eastlands*, which was insured against marine risks under a time policy. The appellants were among the subscribers to the policy. There was no policy covering war risks,

but during the whole of the currency of the policy the period was chartered to the Admiralty, whereby among other obligations the Admiralty assumed all responsibility for war risks and agreed, in the event of total loss from such risks, to pay to the respondents the ascertained value of the vessel at the time of the loss. There were three occasions when the vessel sustained damage from marine risks. She was dry docked, surveyed, temporary repairs were effected to make her seaworthy, but permanent repairs, estimated to cost £1770, were postponed and in fact were never executed. The vessel was torpedoed, became a total loss. The respondents have received from the Admiralty a sum of money which was calculated by deducting from the agreed sound value the sum of £1770 which was the estimated cost of the repairs. Never executed. No dispute as to the appellants' liability for the cost of the temporary repairs. They paid their proportion, but as to their share of the estimated cost of the unexecuted repairs, they dispute liability on the ground they are not bound to pay for damage which, before it was repaired, was followed during the currency of the policy by a total loss.

And the question is whether under a policy of marine insurance the assured can recover in respect of damage sustained by the ship during the currency of the policy when the ship is totally lost before the damage is repaired.

And so that breaks down into two questions: where the loss is caused by a peril insured against by the policy in question, and where it isn't.

His Lordship, on 193 at the bottom, discussed *Livie v Janson*, and half way down 194 says, "Well however you articulate the principle, it is clearly right. If not the assured whose vessel becomes a total loss during the voyage in the course of which she meets a succession of gales, each of which causes damage, would in a case to which section 77(2) of the Act of 1906 does not apply, be in a position to claim under its policies for each of these losses in succession although none of them is or could be repaired and he could at the same time, recover the value of the ship as a total loss if she is wrecked during the currency of the policies. Such a result would, of course, be contrary to the principles upon which marine insurance has always been

executed. The owner would not in such a case merely be indemnified loss but would receive a profit." *Stewart v Steele* case in which *Livie v Janson* was cited and discussed both during the argument and the judgments, Justice Maule in the course of his judgment stated the fundamental principle that the proper time to estimate the loss where a party is put to no expense is at the expiration of the risk." Where the repairs are not undertaken. It doesn't say the cause of action has not accrued because the repairs could be undertaken and if they were, payment would have to be made. But where on the facts of the case a decision is made, not to repair, then this applies. "The principle underlies the decision of Lord Ellenborough and Justice Maule and an earlier passage in the same page says, "It is said that the plaintiff had a vested right of action at the moment of the happening of the loss which nothing could otherwise divest. That I apprehend is quite contrary to the doctrine laid down by Lord Ellenborough in *Livie v Janson*. The learned Judge was of the opinion that inasmuch as the time for assessing unrepaired damages at the expiration of the risk, if the vessel is totally lost before the risk expires, there is nothing upon which such an assessment can be made."

So what Lord Birkenhead is saying is if you repair, you get paid the costs of the repairs. If you don't repair, you get the diminution in value at the end. What you don't have is a chosen action to recover a sum of money that gets treated differently. It is not authority for the proposition that my learned friend put to you, that marine policies of insurance are different from other policies of insurance, because recovery is always postponed to the end of the voyage.

BLANCHARD J:

Is this reference to the voyage? It didn't look to me from what we saw a few moments ago, as if this had anything to do with a voyage. It is a time policy for a particular period. And in that respect, similar to the policy we are dealing with.

MR GRAY QC:

Yes it is the expiration of the risk which is the end of the time.

WILLIAM YOUNG J:

What he is saying, and correct me if I am wrong. But the bit that I was looking at really is at 198 where he, Lord Ellenborough says, "The question in every case must be, did the total loss happen before the underwriters' liability for the unrepaired damage accrued." Bottom left-hand side.

MR GRAY QC:

Yes, yes he did there.

WILLIAM YOUNG J:

And it's very clear that Lord Birkenhead is of the view that in the case of this policy, the underwriter's liability for the damage hadn't accrued before the total loss.

MR GRAY QC:

It hadn't accrued because the repairs had not in fact been undertaken. And so the measure of loss would have been the diminution in value and that didn't arise until the expiration of the policy.

WILLIAM YOUNG J:

There's obviously no provision in this insurance policy, ie the one in *Wilson,* that the insurer was required to pay out on any happening, the amount of the loss or damage or the estimated cost of repairs.

MR GRAY QC:

Whether or not repairs have, in fact, been undertaken.

WILLIAM YOUNG J:

I mean that is the point that Mr Carruthers made, that in this case because of C1 it is perfectly clear that there is an accrued right and it has got nothing to do with whether the repairs are done or not.

MR GRAY QC:

Well my submission on that is that C1 contemplates that the repairs will be undertaken.

WILLIAM YOUNG J:

So your argument really depends on that proposition, doesn't it? I mean if it wrong, then this whole line of argument is wrong isn't it?

MR GRAY QC:

I would prefer to put it that that can be said to be an answer to the line of argument. I don't accept that the policy provides for an accrued right to receive a sum of money without repairs being undertaken, without something being done to trigger that right.

WILLIAM YOUNG J:

So even if I'm happy to say, ell, the building was worth $1 million. Now it's worth 900,000. Here's the valuation. The repairs would actually cost a bit more than that but I'm happy to take $100,000. Do you say that that is a claim that wouldn't be countenanced as a matter of law under this policy?

MR GRAY QC:

Well I don't think you can come along and say, I would have been happy to get $100,000 and therefore I had an accrued right to get one, because the letters shown to you were not, I don't want to do the repairs. It's, I want to do the repairs myself –

WILLIAM YOUNG J:

But give me 197,500 –

MR GRAY QC:

– and you pay for them. Well –

WILLIAM YOUNG J:

I don't think that's right, is it? Let's just have a look at the letter.

MR GRAY QC:

It just says, "We want a cash settlement." It doesn't say whether or not we're going to do the repairs.

WILLIAM YOUNG J:

Well, it does say it will be in full and final settlement of this particular claim.

MR GRAY QC:

Yes, well, of course, a party can say –

WILLIAM YOUNG J:

Sorry, before – no, but –

MR GRAY QC:

– I'm going to make you an offer.

WILLIAM YOUNG J:

– sorry, I'm just picking up the proposition that they were saying, give us the money but you do the repairs, because they weren't. They were saying, give us the money and that's in full and final settlement.

MR GRAY QC:

They're saying, we're not happy with Mainzeal. We don't want Mainzeal to do the repairs.

WILLIAM YOUNG J:

Hawkins, I think, wasn't it?

MR GRAY QC:

Hawkins, I'm sorry. So, boy, have we got an offer for you. Why don't you just give us a lot of money?

TIPPING J:

Mr Gray, I think the key to this case may be whether C1, leave aside C2 for the moment, gives an accrued right on the happening of an insured peril because that was, I agree with Mr Justice Young, that the essential difference between *Wilson's* case and this one may be that in *Wilson's* case there was no accrued right until the end of the period, expiry of the risk, whereas in this case, just looking at it at first blush one would have thought that on the happening of an insured event the insurer becomes liable to pay in terms of C1. The covenant is to pay and if that's not an accrued right, I'd be a bit surprised.

MR GRAY QC:
To pay for repairs.

TIPPING J:
No, to pay for the amount of the loss or damage. That – C1 gives two possibilities to an insured, it seems to me: one to claim the amount of the loss or damage, or to claim the estimated cost of restoring. They may be largely coincident in the mind but conceptually they're different.

MR GRAY QC:
Well, they're different words so they're intended to describe something different.

TIPPING J:
Well, no, it's more than a difference in language. Now why does that not give rise to an accrued liability in the insurer to pay on the happening of an insured event?

MR GRAY QC:
The argument is to come right back to *Castellain* and to the early cases to say what it is that a party to a contract of insured, of insurance is –

TIPPING J:

I don't, with respect, think that answers the point. We all know that you can't get more in insurance than you've lost but the question what you've lost is determined in part at least by the terms of the policy. What you've lost vis-à-vis the insurer is the amount you're entitled to recover under the policy. Now this insured was entitled to recover either the amount of loss or damage or the estimated cost of restoring. I'm forgetting C2 for the moment. Now a covenant to pay on the happening of an event, to my eye, looks like giving the payee an accrued right on the happening of an insured event.

MR GRAY QC:

My answer does become a little bit circular and I acknowledge that. It's because the loss merges, not the claim. Merger is not a doctrine of merger of claims. It's a doctrine of merger of loss and it is that you've no longer suffered loss or damage because the loss or damage merges in the total destruction.

TIPPING J:

So you – at the time of the first earthquake you don't know there are going to be further earthquakes.

MR GRAY QC:

No, you don't.

TIPPING J:

So is it a sense that the claim is valid initially but then overtaken –

MR GRAY QC:

Yes.

TIPPING J:

– by the happening of subsequent events?

MR GRAY QC:

Yes.

GLAZEBROOK J:

And it's actually been explained, if you look at page 190 at 34, by counsel.

TIPPING J:

190?

GLAZEBROOK J:

Of the *British and Foreign Insurance v Wilson*, by saying that under a marine insurance policy you are entitled to the value of, the total value of the ship with no diminution. So in fact you would be being paid twice over in the marine insurance circumstance, if that's right, if you got the partial destruction as well, because you would, you would actually be getting the full value as if there had been no diminution in value. So it actually is a different explanation from the one you're giving. Sorry, I'm at page 190.

MR GRAY QC:

Yes. No, I understand.

GLAZEBROOK J:

Page 34. Now – so that in fact the idea is if it's destroyed you get the value that you've set of the ship. It's probably another way of putting Mr Carruthers' point, in fact, but it seems to be backed up by what's said there, at least by counsel.

MR GRAY QC:

Yes, I understand the point. I don't think there is a response to it. That is in the context of the policy in this case in *Secretan* – sorry, in *Wilson*.

GLAZEBROOK J:

Well, it might be of some assistance to you, I suppose, if you say, well, if you were getting the replacement value you would be being paid twice over, because that doesn't take account of diminution in value.

MR GRAY QC:

And it is this, that the policy then is consistent, that policy underlying the –

GLAZEBROOK J:
So it doesn't help you for your C1 argument, but I don't know that you need merger for the C1 argument, and I was slightly concerned about adding in under insurance issue as well as not already settled and a whole pile of other things that don't seem to be anywhere in the cases.

MR GRAY QC:
Yes, I don't want to –

GLAZEBROOK J:
But it might be that if you say, well, because you're getting a replacement then you don't get the stuff along the way, might have some more legs to it.

MR GRAY QC:
That is our core proposition, Your Honour, and I don't want to be heard to take under insurance too far. There's no evidence in this case about whether under insurance, such as there was, was deliberate or unintentional –

WILLIAM YOUNG J:
But it doesn't have – it's not a warranty of value. It just sets a cap, isn't it?

MR GRAY QC:
Well, it's why we're here –

GLAZEBROOK J:
And under insurance, you just hear the Admiralty insured them for the risk that wasn't insured under the policy and in this case they decide they'll – that this'll do.

WILLIAM YOUNG J:
Everyone in New Zealand now I think will have to be fixing liability caps on their domestic insurance.

MR GRAY QC:
We'll have to get our homes valued.

WILLIAM YOUNG J:
Yes. Well, you don't have to get them valued. You just have to identify a figure, but I don't think that – the only consequence of a figure is that you can't recover more than that. It's not a moral issue. It's not a matter of saying, well, you've under insured, or anything else or you've asserted a value that's untrue. It's simply saying you are accepting this as a maximum cover and you're self-insuring for anything on top of that.

MR GRAY QC:
But the point at which it becomes a moral issue is the Fire Service levy one where people are buying in respect of multiple properties or are taking a risk that they'll have damage but never destruction and are not making the right contribution to Fire Services and other social services and that's where that line of cases took itself.

TIPPING J:
Mr Gray, I'm sorry to keep returning to it but does your argument depend on C1 being premised on the basis that there must be actual repair before there's a liability to pay? Because I have to say that it does. It seems like a very difficult argument.

MR GRAY QC:
It has been, Your Honour. I am now going to go to the lunch break and I will respond to Your Honour after that.

TIPPING J:
Because you may be right but it doesn't look like that at first reading or second reading.

MR GRAY QC:

Well, it's very –

TIPPING J:
The word "estimated cost" doesn't imply that you will actually restore.

GLAZEBROOK J:
Or even the diminution in value, the damage, you may decide to take it and sell it.

MR GRAY QC:
Yes, a wing might be damaged and you might decide to demolish the wing and not replace it.

GLAZEBROOK J:
Or sell the damaged…

TIPPING J:
But hitherto has your argument depended on that particular view of C1 or – if one were to hold that repair, actual repair, was not a precondition or a requirement of C1, why does that, or does that damage your ultimate argument and if so, why?

MR GRAY QC:
No it doesn't because my ultimate argument is that whatever may be the loss or damage, it has merged in destruction.

TIPPING J:
So your premise that C1 is based on actual repair, is a flourish that you do not need.

MR GRAY QC:
It certainly is not –

WILLIAM YOUNG J:

Well you do need it to get round what Lord Birkenhead said don't you?

TIPPING J:

Yes this is the problem, it is the accrual.

MR GRAY QC:

Yes. I say, however, well I have said my argument.

TIPPING J:

Yes I understand but if there is anything new that you can usefully say on it, it is important you should have the opportunity of doing so.

MR GRAY QC:

I do want to finish going through *Wilson* because there are other judgments in *Wilson* that say things.

TIPPING J:

Well I have just been looking at them and some of them are quite helpful.

MR GRAY QC:

We have got to page 195 on 36 of the bundle. The final paragraph, "Such was the state of the authorities at the date when the last edition which was prepared by the author of *Arnoulds* and that work was second edition. The late Mr Arnould stated the law in the following terms, "If a ship has been actually repaired in a port of distress and be afterwards totally lost before arriving at her port of destination, the cost of such repairs may be recovered cumulatively in addition to the total loss, either acquire average or as money laid out and expended in labouring for the safeguard and recovery of the ship under the general printer clause in the policy but the rule only applies repairs actually made. Hence when a ship was put back twice in distress and on the first occasion was actually recovered but on the second was only surveyed but not repaired, and in the course of survey some of her wales etc were necessarily removed in order to examine her but sold with the rest of the ship as a wreck. It was held that the cost of the recovery might be recovered in

addition to the total loss but not the expense of recovering the wales." And then there is debate sale. "It is clear from the footnotes that the learned author did not forget that the subsequent total loss might be from a risk accepted from a policy and that he did not consider that this circumstance affected the liability of the underwriters for unrepaired partial damage. In other words, if after partial damage has been sustained and before it is repaired, the ship is totally lost during the currency of the policy, then in his opinion the underwriter is under no liability for such parcel damage whether he has to pay a total loss or not." And then there is the discussion of *Lidgett v Secretan.* And then over the page, a quarter of the way down, Justice Lindley in *Pitman* made a pronouncement to the same effect as that of Justice Willes and Mr Wright also admitted that if this opinion was in law, well foundered, the respondents in this case were wrong. *Pitman's* case turned upon the question that what is the true principle upon which an unrepaired loss is to be estimated. In the course of his judgement, Justice Lindley remarked, "Against what do the underwriters agree to indemnify the insured. Surely as against such loss as he may in fact sustain by reason of the perils insured against. That this is so is plainly proved by those cases which decide that where a ship has been injured and not repaired, the assured must wait to the expiration of the risk before he can sue the underwriters for the loss he has sustained, the insured has no vested right of action where the injury is sustained. If in such case the ship is lost while the policy is running by a peril not insured against, the assured has no right of action at all and if she is lost by a peril, insured against the assured can only claim for a total loss, he cannot claim both. And then His Lordship sets out the rule. The classic statement of the rule is on 199 in the second to bottom paragraph. On 200 Your Honours, is the judgement of reasons for decision of Viscount Finlay which agreed. On 205 is Lord Shaw, a brief judgment but the final paragraph of it is also a good summary and it deals with the claim to money argument. His Lordship said, "My Lords when a ship damaged but only part –

GLAZEBROOK J:

Sorry I need to find this.

MR GRAY QC:

207 Your Honour. "My Lords when a ship damaged but only partly repaired is totally lost, it, of course, becomes impossible to complete her repair. No contract of indemnity can apply to being recouped for such repair because that would be to present a false and impossible demand for indemnification, that is, indemnification for an expenditure which can never be made. If, once the principle of indemnity were extended the length of permitting a mere right of action to be on the ground on the measure of the indemnity, then the reality of the case is lost sight of, for the right of action is a mere abstraction and represents in truth a right to be recouped for the expenses which can never be laid out, and the word 'indemnity' or the word 'recouping' failed on account of sheer self-inconsistency. One finds oneself not in the region of indemnity against loss, but in the region of profit taking. This is contrary to all sound principles of marine insurance, and apart from all those authorities which have been most properly canvassed, I am of the opinion, on the principle I have just stated, that this appeal should succeed."

And to similar effect Lord Moulton, on 208, in about the middle of the page, having discussed *Livie v Janson*, says, "The only alternative to that decision would have been to hold that when damage was done by perils insured against there instantly accrued a pecuniary claim against the insurer for the estimated cost of the repairs whether done or undone, a doctrine which, among other things, would have led to the absurd result that all the damage done to a ship immediately before or in a storm in which she was totally lost might be claimed as particular average by an owner who had not insured against total loss."

And then His Lordship's decision is over at 210 in the long paragraph, which is repetitive, basically saying that war risks were a matter for the owner. Lord Sumner explains his understanding of *Livie v Janson* at 212 in the second paragraph. "Lord Ellenborough's language does not mean that two conditions must concur to relieve an underwriter from liability for unrepaired damage; first, the occurrence of a subsequent total loss and, second, an absence of any pecuniary interest whatever in the unrepaired partial loss.

The words, ‘And the previous deterioration becomes ultimately a matter of perfect indifference to his interests,’ explain the effect which the subsequent total loss has on the prior unrepaired damage, and so justify the rule.”

And His Lordship deals with under insurance on 214 in the second paragraph. It says where there is under insurance, the insured is treated as being self-insured for the uninsured portion.

Now that completes a consideration of *Wilson*, Your Honours, and it’s 1 o’clock.

GLAZEBROOK J:
Can I just check with you whether there was anything equivalent to the Marine Insurance Act 1906 for other insurance?

MR GRAY QC:
No. The Marine Insurance Act, which is now largely of historical interest because most of its provisions are matched by common law decisions, was the work of some enthusiasts in the market, two or three of them only, and was drafted really to gather together the understanding of the meaning of a particular form of policy which was called a, a something or other. No one knows the origin of the name. It just was a form of words which was in common usage. There was a common understanding of what the words meant and the Act was intended to codify them.

McGRATH J:
Mr Gray, can I ask you, what are you going to be taking us to following luncheon?

MR GRAY QC:
Not much, Your Honours, just the differences between marine insurance and other insurance.

McGRATH J:

Thank you. Adjourned to 2.15.

COURT ADJOURNS: 12.59 PM
COURT RESUMES: 2.18 PM

MR GRAY QC:
May it please Your Honours, to wrap up the submissions I was making before luncheon to respond to the questions that had been asked, focusing on clause C of the policy, which is at page 79 of the bundle, our submissions are these. First, that clause C deals with the amounts that can be claimed. It's a quantum provision. Second, that for damage short of destruction, clause 2 does not apply because clause 2 requires restoration or replacement and that has not occurred and cannot occur, and that's what the Court of Appeal found. So that for damage rather than replacement, we're not in clause 2. We have to be in clause C1. So far as clause C1 is concerned, we say that 2 contemplates actual replacement by reason of the use of the words "loss" or "damage" and cost of restoring, contemplating moneys actually spent, and those are our submissions about what that means. Of course, in this case there will be –

GLAZEBROOK J:
So that's – because didn't – I see, because you say the Court of Appeal found that it was because it was destruction it was under clause 2, is that…

MR GRAY QC:
They found initially that the claim was not articulated under clause C1.

GLAZEBROOK J:
Yes.

MR GRAY QC:
And they said it's a claim under clause C2, and then they said because it's a claim under clause C2 and because clause C2 for damage requires restoration or replacement then there can no longer be a claim for damage or

replacement under clause C2. That's the way the Court of Appeal came to its decision.

GLAZEBROOK J:
I'm really just trying to see where you disagree or agree with the Court of Appeal. That was –

MR GRAY QC:
I agree that –

GLAZEBROOK J:
Sorry, I put that question badly. That was the…

MR GRAY QC:
Look, I don't take the pleading points, Your Honour.

GLAZEBROOK J:
Right.

MR GRAY QC:
I accept that this is a preliminary question and my learned friends would be entitled to amend their claim if they wanted to, in the light of the answer, of course, to the preliminary question, and I, with respect to the Court of Appeal, say that it's a little bit artificial to try and confine the plaintiffs to a C2 claim when, in my respectful submission, the pleadings are not quite as clear as the Court of Appeal may have said and there are always the options for amendment.

I do agree with the Court of Appeal that if the – to the extent that the claim is under C2, it requires replacement or restoration. That's no longer possible so that for damage there can no longer be a C2 claim, and, of course, for loss –

WILLIAM YOUNG J:
But that's not true. It could be replaced somewhere else.

MR GRAY QC:
No, no, no. That's for destruction, Sir.

WILLIAM YOUNG J:
Sorry, if unable to be repaired because of such damage, the cost of replacement by an equivalent building.

MR GRAY QC:
It's been paid.

WILLIAM YOUNG J:
Okay, sorry, well, I understand what you're saying. You're saying because it's been paid that's okay, but absent payment and subject to the cap, C2 was able to apply.

MR GRAY QC:
Sir, I was talking about damage, not destruction.

WILLIAM YOUNG J:
Right.

MR GRAY QC:
C2(a)(i) applies to damage. C2(a)(ii) applies to destruction. Clause C2(a)(ii) can and did apply to destruction, and that's why I was differentiating, Your Honour, between damage and destruction.

WILLIAM YOUNG J:
Okay, thank you.

MR GRAY QC:
So within C1 we say there has been no loss because of mergers and there are, of course, factual issues remaining about the extent to which the appellants in this Court have acquiesced in repair by the respondent, a matter

referred to by Justice Dobson in his judgment in paragraph 16. 64, I think it is, Your Honours. While His Honour knew about the letter that's at –

WILLIAM YOUNG J:
Have you got a page reference?

MR GRAY QC:
48, Your Honour, in the case. His Honour had been shown the letter, that is page 100, and he said, "Well, yes, but hang on, work was undertaken, work was paid for, the insured didn't stop that, didn't get in the way of it, didn't try and prevent it happening."

WILLIAM YOUNG J:
Well, we can't deal with this now, can we?

MR GRAY QC:
No, no. It's a factual question, Your Honour, and all I'm saying is those factual questions will need to be left for the next phase. And we say the doctrine of merger is a doctrine of merger of damage.

McGRATH J:
Yes.

MR GRAY QC:
And that really brings me, Your Honours, to the arguments made by our learned friends that the law of marine insurance is so different in material respects from the law of general insurance or material damage insurance that marine insurance cases don't apply. I apprehend our learned friends' arguments may have been overtaken somewhat by argument in Court today and by a close analysis of what it is that the authorities have been saying, but if and to the extent that a general proposition is made then we say there in fact are only three main differences between marine and other insurances. The first is a recognition of constructive total loss and that's not something which applies in this case or by itself as a ground for saying the marine

insurance cases that we have been looking at, should not apply to fire and general or material damage policies. And second that it's the practice but not the law for whole policies to be valued policies and what we say about that is some are and some aren't, and equally in material damage policies, some are valued and some are not. Again that is not a characteristic of insurance which actually affects the propositions that we have been looking at.

WILLIAM YOUNG J:

Well in a, I suppose we might call it a vanilla marine insurance case where the insured property is valued. Unless you had a version of the rule that came out, an insured would get more than had been lost if you could treat two incidents separately and that is why the rule developed and then the rule had to be applied in different situations where the underlying policy wasn't quite so obviously engaged.

MR GRAY QC:

Even in valued policies, it was possible for an insured to recover more than the value.

WILLIAM YOUNG J:

How?

MR GRAY QC:

By having repairs actually undertaken and paid for, so that the damage does not merge and then the vessel being lost.

WILLIAM YOUNG J:

Oh I see.

MR GRAY QC:

So in our respectful submission Sir.

WILLIAM YOUNG J:

Well it doesn't really recover more than the value because at the end of the day the insured would otherwise be out of pocket for the repairs.

MR GRAY QC:
That's right but if the value is treated. I mean the value is not necessarily a cap and I suppose the point is that caps and values are different.

WILLIAM YOUNG J:
Yes.

MR GRAY QC:
And the third is that average applies in marine insurance and of course average does not apply to material damage policies in New Zealand unless specifically included. Again it is not a factor which is relevant in this case and look if you do word searches for marine adventures, you find that the phrase is not used in the Marine Insurance Act provisions dealing with indemnity, is not relevant to the scope of the indemnity provided by policies of marine insurance.

WILLIAM YOUNG J:
Sorry, what word isn't?

MR GRAY QC:
Marine adventure. Maritime adventure. We only turned up one case in the last 100 years which relied on the phrase and that was on a wholly unrelated question of whether or not a voyage had been for an illegal purpose so that the warranty of legality could be complied with and then it was analysis of whether the adventure was illegal or whether the means of performing it was illegal. And that is a case called *Sea Glory Maritime Co & Swedish Management Co SA v Al Sagr National Insurance Co (M/V "Nancy"*) [2013] EWHC 2116 (Comm) that is in one of our footnotes but needn't have troubled Your Honours. So we say that the proposition that, because the cases that we have been relying on arise in the field of marine insurance and because marine insurance is so different from material damage situations, therefore the

cases don't apply, isn't helpful. But I do appreciate that in discussion today we tended to overtake that by looking more closely at the authorities themselves and it may be that that general point becomes subordinated to the specific ones that we have been talking about.

So if it pleases Your Honours, we rest our case really on this proposition that policies of insurance are intended to indemnify people for the losses that they suffer and where the losses that they suffer are incapable of being repaired, before they merge in total loss and there has been indemnity for total loss, then the loss rather than claims have merged, and that that provides an answer in this case. If on the facts of this case we end up with a contract to repair, then that does bring us into the territory of *Wright, Stephenson* but in our submission, what discussion today has shown is that *Wright, Stephenson* is sound, that *Wright, Stephenson* did come to the right answer on the facts of that case, particularly the terms of the policy in that case and that there is no reason for this Court to be concerned about whether *Wright, Stephenson* might have been correctly decided. The question for Your Honours' determination is whether by reason of the peculiarities in the doctrine of merger, it doesn't apply to the facts of this case but the proposition, albeit an obiter proposition, in the Court of Appeal that there is no obvious reason to confine the doctrine to marine insurance law, we submit is a sound one and on the facts of that case, the analysis that the contract to repair had been frustrated also was sound. It was impossible on the facts of that case to repair the car as it is now impossible to do the repairs to this building, but we are offering a different doctrinal solution to the conundrum post.

TIPPING J:
If the lost suffered is measured by the cost of repair and the repairs can't be affected, does that affect a situation where the loss suffered is measured by diminution in value because your diminished value can still be calculated.

MR GRAY QC:
And if it was accrued, then yes it could be calculated and paid. Alternatively it could merge in destruction if it hasn't accrued.

GLAZEBROOK J:

But what would you get for destruction in that case, wouldn't you get the value of the building less the costs of repairs, so the insured would be out of pocket?

MR GRAY QC:

In my submission it is implicit in merger that you get the value of the whole of the building. The doctrine is that all of the damaged mergers into the whole and you get the value of the whole, not a diminished value because at the precise moment bits of it had already been damaged.

GLAZEBROOK J:

If your insurance policy says you get the value of the building at the time it is destroyed, how can the value of the building be anything less than the value of the building at the time it is destroyed? How can it suddenly increase in value because of the doctrine of merger?

MR GRAY QC:

My answer to Your Honour's question is this. That that is an analysis that looks at the claim.

GLAZEBROOK J:

Well I prefer actually, in any contractual situation which insurance companies seem to have great difficulty in, is actually looking at the terms of the actual insurance policy that we are talking about, rather than speaking in generalities about what happens in insurance.

MR GRAY QC:

I can't accept the general, I haven't been here in any other cases. But what we say in this case.

GLAZEBROOK J:

But how does it override the terms of a contract is what I am really asking?

MR GRAY QC:

I think what it does is treat four events, all of which occurred in a policy period, none of which was able completely to be addressed by the time of destruction and simply settle them altogether, as one loss.

TIPPING J:

Yes well I was contemplating the concept if you consolidate the loss, into the one loss at the end of the day.

MR GRAY QC:

That's a way of expressing it.

TIPPING J:

Well that is the same as what your – I am not saying that is my view but that is one way of looking at it, a sort of consolidated loss. You can't get paid for the same damage twice.

MR GRAY QC:

No you are entitled to be paid for all of the damage but you don't get paid for any of it twice and neither should you, is our submission.

WILLIAM YOUNG J:

What was the indemnity value of the building when it was destroyed, do you know?

MR GRAY QC:

No I don't have the actual value, Sir.

WILLIAM YOUNG J:

Could it have been as high as the $1.9 million?

MR GRAY QC:

Oh in it's damaged condition.

WILLIAM YOUNG J:

Well let's say, what would the indemnity value of the building be, say as at the beginning of September 2010.

MR GRAY QC:

There was a proposal Sir. I don't know that the record tells us, is the point Your Honour. No I am sorry Your Honour, there is nothing before the Court and I would be speculating.

WILLIAM YOUNG J:

Say it was around, that even as damaged, it still had an indemnity value of perhaps $2 million. Wouldn't – how would you treat merger then, because then you'd all be entirely under C1? The claim could be brought under C1 and would be, as it were, still engage the cap.

MR GRAY QC:

Yes, that's possible. If the damaged condition of the building before whichever earthquake destroyed it exceeded 1.9 then C1 could apply, and absent the merger of loss that I've been making submissions about, then C1 could apply.

WILLIAM YOUNG J:

So do we know that that isn't…

MR GRAY QC:

I don't think on the facts we do know. We do know that the plaintiff claims a few hundred thousand dollars for each of the September and December earthquakes, 1.9 million for damage short of destruction in February –

WILLIAM YOUNG J:

Yes.

MR GRAY QC:

– and a further 1.9 for destruction in June.

WILLIAM YOUNG J:
Yes.

MR GRAY QC:
Unless Your Honours have any more questions, those are my submissions.

McGRATH J:
Thank you, Mr Gray. Now in reply, Mr Carruthers.

MR CARRUTHERS QC:
May it please Your Honours, I have five short points in reply. The first is this, that my learned friend has emphasised throughout the principle of indemnity and spoken in terms of the concept of indemnifying for loss suffered. With respect to his argument, that begs the question, and the fundamental question is to interpret the policy correctly, and I don't want to rehearse the argument I made but I draw attention to clause C1 because it provides that the insurance will pay the amount, so it is payment of the amount of loss, and – of loss or damage to, or the estimated cost of restoring. So it does involve a concept of liability to pay an amount and that amount is measured in one – against one of three particular ways.

Now despite my friend's submission to the contrary, that clause does not contemplate that repairs will be done. It's open to the insured to take the money with the amount paid and deal with it. That argument about the scope of liability applies to each of the four separate events.

Now the second submission is that there is no contemplation of duplication of loss or damage one event to another. That is made clear by the agreed statement of facts, and if I can just quickly take you to pages 67 and 68 of the case. At paragraph 2 on page 67, as a result of what was the first earthquake the building suffered damage. These are agreed facts. Paragraph 4, there was a second earthquake that caused further distinct damage to the building

and the same approach to the agreed statement applies to the third earthquake, which is at paragraph 7, further distinct damage, and then at paragraph 9 for the fourth earthquake, and I think I've made it clear throughout that part of my case is that I will have to prove, if I'm successful on this appeal, I will have to prove in relation to each event the scope of the damage in order to justify the claim for the amount of the estimated cost of repairs.

Now that, the agreed statement, is carried through into the preliminary question at page 70, in paragraph 2, "Each happening caused damage to the plaintiff's building," leading to paragraph 6, "Is the plaintiff entitled to be paid for the damage resulting from each happening up to the limit?" So it's not a matter of paying time and again for broken windows as my learned friend suggested. There are four distinct events, four distinct items of damage that need to be proven, and that little summary that I gave you indicated the separate nature of the damage on the events.

The third submission in reply is this, that my fundamental argument is that there is no room for the concept of merger in an event policy and the reason for that is that the policy deals with any loss, damage or estimated cost of repairs, event by event, so there is no room for the concept of merger in the way in which my friend argues for. And that is probably the explanation for the comment in *Crystal Imports*, and this is my fourth submission, Your Honours, just to draw attention to Justice Cooper's conclusion in *Crystal Imports*. If I can take you to the authorities in volume 1, at page 171, where His Honour begins the discussion of merger and deals with a submission that was made by one of counsel for the plaintiff, where His Honour says, "Ms Rosic is correct –

McGRATH J:
What paragraph are you in?

MR CARRUTHERS QC:
I'm in paragraph 99 on page 171 of the authorities.

McGRATH J:
Thank you.

MR CARRUTHERS QC:
"Ms Rosic is correct that there are no reported cases in which the doctrine of merger has been applied to insurance claims other than those arising in the context of marine insurance. The question however is whether the doctrine must necessarily be confined to that context by reason of the inherent nature of its subject matter." And, Your Honours, you may recall that His Honour noted in an early part of that his reasons for judgment that the policy he was concerned with was not an event policy.

The fifth and final submission is just a short point that really doesn't arise particularly for consideration or judgment by Your Honours, but my learned friend was justifying the position concerning repairs on the basis that there was no opportunity, the insurer was overwhelmed, there was difficulty getting contractors. That doesn't quite capture what the insurer is saying. I won't tarry with it but at page 116 of the case, and you'll see in the second to last entry, the Fritz Muller entry, 11 October 2010, I drew attention to the storm damage. "The insured called to inform that storm damage last night damaged temporary cover on roof and requests permission to do more permanent repair until the claim is settled and two or three of the tenants might move out and authorised repair." Now part of the evidence will be that those involved with the appellant were experienced property owners and had the ability to do repairs themselves, and part of the issue on the facts concerns the carrying out of repairs and you'll recall that I took you to that exchange at page 100 concerning the acceptability of Hawkins and the response on page 101 suggesting that the insured had, have no rights in that respect. So it's not entirely correct to say that there's the issue of repairs was something that the insurer had completely in its control and that the insured had no role because there is very much an issue for trial on that point.

Your Honours, unless there are any other matters that you specifically want me to deal with, I'll just be repeating my submissions.

GLAZEBROOK J:
Can I just ask you something that I asked Mr Gray, that if you do look at a replacement under C2 –

MR CARRUTHERS QC:
Yes.

GLAZEBROOK J:
– why are you not in exactly the same position as the marine cases where you might be paying over again for repairs that haven't been done? This is ignoring the cap for a moment.

MR CARRUTHERS QC:
Yes.

GLAZEBROOK J:
Let's assume that the cap is equal to the replacement value, so for the purposes of this question.

MR CARRUTHERS QC:
Right. Because I will, under my three previous claims, have been paid the estimated cost of my repairs and on my fourth claim I am paid my estimated cost of repairs so that I have a fund that goes towards my replacement cost and I am entitled to my replacement cost up to the 1.984 million and I am entitled under the policy to top up the difference between my old for old to "as new" on my four claims. Now the difference, Your Honour, is simply in the terms of the policy, the nature of the policy, because it is as the insurer has drawn it and wanted it, an event by event policy, and that's the distinction from the marine insurance cases.

TIPPING J:

Just on point, Mr Carruthers, if I may. It seems a little capricious that if you have managed to get the repairs done, there can't be, if you like, merger, and this point may help you.

MR CARRUTHERS QC:
Yes.

TIPPING J:
I don't know whether it does or not. If you've managed to get the repairs done in time then that is no longer a loss that is capable of merging. But if you haven't managed to get it done in time, that is a loss that is capable –

MR CARRUTHERS QC:
Yes.

TIPPING J:
– of merging and it just seems slightly unsatisfactory that it should differ.

MR CARRUTHERS QC:
Yes. Well, with respect, I agree, and Your Honour may recall in that short summary I did at the end it was that factor that I just took into account, that it seemed anomalous that if you had the opportunity to repair then that was paid but if you didn't then that wasn't paid, and yet conceptually one is talking about exactly the same loss, damage or estimated cost of repairs, so –

BLANCHARD J:
Except if the repair's been carried out you've lost all over again –

MR CARRUTHERS QC:
Yes.

BLANCHARD J:
– when the destruction occurs.

MR CARRUTHERS QC:

Yes, yes, that's so, and –

BLANCHARD J:

Whereas arguably if you haven't done the repairs, yes, you did have a prior loss but, subject to the arguments you're making –

MR CARRUTHERS QC:

Yes.

BLANCHARD J:

– it's overtaken by the destruction.

MR CARRUTHERS QC:

Yes, but the answer to that must be that it was an accrued right at the time the damage occurred.

BLANCHARD J:

I understand the argument.

MR CARRUTHERS QC:

Yes, yes. I think that's the only answer that I can give, Your Honour, to the proposition you've put to me though.

TIPPING J:

But I think my brother has put his finger on why it's not anomalous –

MR CARRUTHERS QC:

Yes.

TIPPING J:

– to have a different consequence accruing from making the repairs and not making the repairs, which was slightly troubling me, but I think the point is fully answered by my brother's observation that you've lost it all over again if

you've done it, and then there's another event which destroys the whole caboodle.

MR CARRUTHERS QC:

Yes. Well, I think the only answer I can give to that is that is a feature of the way in which the policy is drawn, that that's the consequence that necessarily follows, which is a result that falls on the insurer.

TIPPING J:

In a sense it might help you in that – well, no, I won't pursue it, Mr Carruthers, I think. That's for me to ponder on, I think, rather than trouble you with.

MR CARRUTHERS QC:

Thank you, Sir.

McGRATH J:

Thank you, Mr Carruthers. Thank you, counsel. We will reserve our decision.

COURT ADJOURNS: 2.52 PM