IN THE HIGH COURT OF NEW ZEALAND
CHRISTCHURCH REGISTRY

CIV 2013-409-001511
[2015] NZHC 1444

BETWEEN	PRATTLEY ENTERPRISES LIMITED Plaintiff
AND	VERO INSURANCE NEW ZEALAND LIMITED Defendant

Hearing: 1-5, 8-12 December 2014, 9-10 and 12-13 March 2015

Appearances: FMR Cooke QC with S P Rennie for Plaintiff
D J Goddard QC with SWB Foote and C M Brick for Defendant

Judgment: 24 June 2015

JUDGMENT OF DUNNINGHAM J

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Introduction

[1] In the heart of Christchurch, just east of Cathedral Square, stood the plaintiff's building, Worcester Towers. Like so many of Christchurch's older buildings, it was progressively damaged by the earthquakes of 4 September and 26 December 2010, and 22 February 2011. It could not be reoccupied after the Boxing Day earthquake and, in June 2011, the Canterbury Earthquake Recovery Authority issued a notice requiring its demolition.

[2] Such facts have given rise to a number of insurance law cases to determine the insured's right to cover under its policy, especially where a building is affected by multiple earthquake events. This would be one such a case but for a further complication. In August 2011 the plaintiff, Prattley Enterprises Limited (Prattley), agreed to resolve its claim for material damage to Worcester Towers on payment of $1,050,000 plus GST, less the insurance excess, in "full and final settlement and discharge of the claim" ("the Agreement"). I must therefore determine whether there are circumstances which make it unfair to hold Prattley to the Agreement, before I can decide whether it is entitled to any greater sum under the terms of the policy.

[3] Prattley's position is that its insurer, Vero, did not comply with its contractual obligations to correctly explain Prattley's entitlement under the contract of insurance. It says Vero misrepresented to Prattley that its entitlement was measured by the market value of the building, when it fact it was entitled to the cost of reinstatement on each of the 2010 earthquake events, plus the depreciated replacement cost of the building on the third earthquake event in 2011. While each of those payments would be subject to the agreed indemnity value cap of approximately $1,600,000, Prattley would have been entitled to significantly more than it settled for.

[4] Vero's position can be summarised by saying that the Agreement is valid and binding. Prattley entered into it in reliance on its own independent advice and, in any event, there are sound policy reasons to uphold the effectiveness and integrity of settlement agreements. In any event, it was not wrong in the context of a policy which ensures a building on an indemnity basis to measure the insured's loss as being the market value of the building.

[5] To resolve the issues in dispute I must determine:

(a) Vero and Prattley's legal obligations and entitlements under the contract of insurance;

(b) the damage suffered by Prattley as a consequence of each insured event;

(c) the correct measure of Prattley's loss as a consequence of the damage suffered;

(d) if Prattley's entitlement under the policy exceeded what was paid under the Agreement, whether any of the following grounds exist to justify reopening the Agreement:

(i) Vero breached its obligations under the contract, including obligations it had under the Fair Insurance Code;

(ii) the Agreement was not a true contract of compromise;

(iii) the Agreement was reached in breach of the Fair Trading Act 1986;

(iv) the Agreement was entered into because of a qualifying mistake under the Contractual Mistakes Act 1979.

[6] With those issues in mind, I outline the relevant factual background.

The factual background

The building

[7] Worcester Towers was located at 103-105 Worcester Street next to the Cathedral Junction development. It was built in the 1920's and comprised three storeys and a basement, arranged in two main wings which were connected at the rear of the property. An historic Edwardian building which had stood on the front of

the site, had been demolished in 1984 and the cleared space allowed for tenant car parking. At the same time a concrete block stairwell was added to the front of the west wing and some other strengthening work was undertaken to other parts of the building, although this was not comprehensive strengthening work.

[8] The building was one of several buildings owned by the late John Britten, who was well known because of his development of the revolutionary Britten motorcycle. The building housed the Britten Motorcycle Company and Motorcycle Museum, as well as a range of commercial tenants, the most significant of which was the Metro Theatre which operated a boutique theatre complex in the east wing of the building. The income received from the building was used to support the Britten family.

Management of Prattley

[9] On John Britten's death in 1995, his assets, including those held by the companies he owned such as Prattley ("the Britten Group companies"), were transferred to the trustees of Mr Britten's estate. The four trustees comprised Mrs Kirsteen Britten, his wife, Mr Bruce Irvine, a highly experienced accountant and company director with legal qualifications, Mr Chris Weir, a senior partner of a large commercial law firm, and Mr Timothy Corcoran, a retired lawyer and company director.

[10] While Mrs Britten and Mr Corcoran were the directors of Prattley, it was uncontentious that major decisions for all estate assets, including those held by Prattley, required approval of the trustees. The trustees were assisted in the day to day running of the estate by Mr Ray Minehan, who was engaged to manage the Britten Group properties, and Ms Eileen Yates, who was responsible for general administration of the Britten Group companies.

Placement of insurance

[11] The insurance needs of the Britten Group companies were, from December 2009, handled by Ms Karen Austin of Amicus Brokers Limited. She dealt with Mrs Britten, Ms Yates and Mr Minehan to arrange insurance for

Worcester Towers, and three other commercial buildings owned by the Britten estate, as well as for the residential houses owned by Mrs Britten, and for associated contents and motor vehicles.

[12] At the time Ms Austin took over, there were discussions regarding whether the commercial buildings should be insured for indemnity value or reinstatement cost. In the end Ms Yates advised Ms Austin that replacement cover would only be required for the newest of the four Britten Group properties, being a building in Hereford Street, and the balance would continue with indemnity cover, because the trustees "would not want to pay the extra premium for reinstatement cover".

[13] A quotation was sought from AMP,[1] for insuring Worcester Towers for loss of rents, material damage and property owner's liability cover. The insurer responded by requesting that the following wording be included before insurance cover was offered: "We will repair or reinstate the building to as reasonably equivalent appearance and capacity using the original design and suitably equivalent materials". That endorsement was requested because it was wrongly assumed the building was a protected heritage building and Ms Austin understood this was to ensure the insurer did not have to source or pay for old or difficult to obtain building products. Insurance cover was duly obtained on that basis commencing 21 December 2009.

The insurance claims

[14] The 4 September 2010 earthquake struck before the policy's first renewal date. Some visible damage to Worcester Towers resulted but, apart from one tenant, the tenants stayed in the building and continued to pay rent. A claim was lodged with Vero, and Prattley engaged engineers from Eliot Sinclair Limited to inspect and report on the repairs required. The engineer's report was not completed when the 26 December 2010 earthquake struck. That earthquake caused more significant damage to the building and, again, Eliot Sinclair was engaged to provide a report on the damage. The Christchurch City Council red-stickered the building, meaning it was not considered safe to occupy.

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[1] AMP was the insurer's name at the time, but it became Vero and all subsequent references will be to Vero, although at times the evidence referred to AMP.

[15] Following the Boxing Day earthquake Mr John Henry and another engineer from Eliot Sinclair provided a report on the level of damage in Worcester Towers. The report concluded that the building had suffered serious damage, and the damage from the Boxing Day earthquake was much greater than that from the 4 September earthquake. The structural integrity of many of the building's walls was substantially compromised by cracking, and the earthquakes revealed that a number of corner junctions in the building had not been bonded or interwoven but were only butt jointed, and so were "vulnerable to collapse in strong earthquake shaking". For these reasons the building was clearly not safe for occupation.

[16] The report outlined the key remedial work which would be required to allow reoccupation. However, even for short term reinstatement and reoccupation by tenants, this work would likely require three to six months to complete. A longer term solution would require significant stripping of the internal fitout to expose the basic building fabric and structure. It was unlikely it could be tenanted during that work. However, overall, the engineers concluded that "the building has been so seriously damaged that repair and strengthening of the building is unlikely to be a viable proposition".

[17] Again, an insurance claim was lodged in respect of the Boxing Day earthquake, but no other work had been undertaken when the 22 February 2011 earthquake occurred. In that seismic event, the top level of the neighbouring Press building fell onto the roof of Worcester Towers and sections of the roof and upper floor collapsed. The only time the building was entered after that was to retrieve a famous John Britten motor cycle.

[18] On 1 March 2011 the Council informed the trustees that the building was to be demolished and, on 9 June 2011, the building was made subject to an order under s 38 of the Canterbury Earthquake Recovery Act 2011. It was subsequently demolished in September 2011.

[19] Naturally, a further claim was lodged in respect of the February earthquake. The second two insurance claims were made under the renewed policy which ran from 21 December 2010 through to 21 December 2011.

How did the parties negotiate the Agreement?

[20] Mr Derek Cherry was the Vero representative who handled the Britten Group's claims at the relevant times, including negotiating the Agreement on which the Worcester Towers claim was settled. His first contact with Prattley's representatives was when he spoke to Mr Minehan in late May. It was made clear to Mr Cherry that the Britten Group companies were unhappy with the way their various claims were being progressed. As a consequence, he agreed to review them and to move them forward, and he became their point of contact at Vero.

[21] On 14 June 2011, when it was known that Worcester Towers was to be demolished, he attended a telephone conference with Mrs Britten, Mr Minehan, Ms Yates and their broker Ms Austin.

[22] However prior to that meeting the Britten Group representatives had done some homework. As early as mid-January a decision was made by Prattley to engage Ford Baker to undertake a valuation of Worcester Towers. That was undertaken and a valuation was sent to Mr Minehan on 6 May 2011. It was described as being a "pre-loss market indemnity value", and it used three methodologies to arrive at a "market indemnity valuation"; depreciated replacement cost, investment valuation (based on capitalisation of rental) and present value of rental income. It concluded that, having regard to the three valuation methods, the appropriate market indemnity value of Worcester Towers was $700,000. Ms Yates' report to the trustees on 7 June 2011 recorded that a valuation for Worcester Towers was received but "[i]t is probably not favourable for our claim. We will shelve this for now".

[23] On 10 June 2011, Ms Yates emailed Mr Weir, one of the trustees and a commercial lawyer, to check Prattley's insurance entitlement. She provided him with the schedule to the insurance policy and asked whether the insurer had an obligation to pay out the indemnity value of $1,605,000, or whether that amount was only payable if Prattley rebuilt, saying:

> … they have after all accepted the policy and we have paid premiums based on that amount.

> Or is that amount only applicable if we rebuild?
>
> They mentioned that they are getting a valuation. We are meeting with them next Tuesday. I know our valuation does not support the $1.6M.

[24] Mr Weir referred her query to be considered by another lawyer in his firm. That lawyer in turn requested the complete insurance policy document and clarification as to whether the earthquake indemnity MD020 extension applied, or the earthquake reinstatement cover MD022 extension applied, so that the firm could respond to Ms Yates' questions.

[25] None of these matters were disclosed to the insurer at the 14 June 2011 telephone conference. Instead, Mr Cherry agreed that he would promptly obtain a valuation to assist in establishing the indemnity value of the building. The very next day he instructed Knight Frank, another firm of valuers, to undertake a valuation of the Worcester Towers building, noting that he needed "an indemnity value as at 04/09/2010". He explained that his understanding was that "[u]sually this is a market value of the improvements with a comparison of replacement less depreciation".

[26] On 21 June 2011, and before there was any further communication from the insurer, Ms Yates' and Mr Minehan received advice from Mr Weir's law firm about Prattley's entitlement under the policy. While the advice was primarily intended to answer Ms Yates' questions about whether the indemnity value limit in the policy of $1,605,000 was payable, and whether Prattley would be paid only if it rebuilt, the advice also provided an explanation of Prattley's entitlement under the policy.

[27] The advice explained that earthquake cover was provided if one of two additional extensions applied, being earthquake indemnity cover under MD020 or earthquake full re-instatement cover under MD022. Although the advice expressed a concern that earthquake cover did not apply on renewal of the policy, on balance, it concluded that MD020 earthquake indemnity applied throughout, but the cover was limited to the total sum insured.

[28] Importantly, the advice concluded:

> In any event, given that the Towers has been destroyed, the maximum amount of cover will be no more than the value of the building at the time it was destroyed (which may be less than the total sum insured).

[29] The legal advice also confirmed that there would be no requirement to rebuild Worcester Towers in order for Prattley to be compensated for its loss under the policy.

[30] Having received that legal advice, Prattley awaited the insurer's valuation, which was chased up by their broker Ms Austin.

[31] The Knight Frank valuation undertaken by the insurer was forwarded to Vero on 6 July 2011. It showed the market value of the land and buildings before the earthquakes was $1,870,000. Given the land value was assessed to be $1,500,000, the pre-loss market-based indemnity value of Worcester Towers was $370,000. Alternatively, using a depreciated replacement cost approach, the value was assessed at $1.4 million.

[32] Mr Cherry sent the valuation to Ms Austin the next day and asked her to forward it on to Prattley. Ms Austin came back to him by email on 12 July 2011 asking whether he had any advice as to which method of settlement would be used to settle the claim, as the depreciated replacement value was much higher than what she described as "indemnity value". She also asked whether, if Prattley wanted to obtain a second valuation, the insurer would pay the cost of that.

[33] Mr Cherry emailed Ms Austin the next morning with his response. He advised that the policy provided an indemnity to compensate the property owner for their loss. He explained this as follows:

> Often this involves the actual cost of repairs less an appropriate allowance for betterment. But where the property is in fact destroyed, the market indemnity value is typically the outcome. This compensates the owner for the actual value of the improvements so that they are in a neutral position. They still have the land and cash equivalent to investing (sic) in a similar property elsewhere yielding the same returns. In this case, the valuation is low compared to the depreciated value and the sum insured. It is also below the owners expectations. I am discussing this situation internally this week and will advise the outcome.

[34] He went on to agree to pay for a second valuation of the insured's choosing (although he said it was not usual), and he invited Ms Austin to share the email with Prattley if she chose to.

[35] In the meantime, and unbeknown to the insurer, Prattley's representatives had been focused on obtaining a "better" valuation from Ford Baker than the 6 May 2011 valuation by providing rental figures which assumed all the building was occupied, and all rents adjusted upwards on the basis of assumed rent reviews, and ignoring the fact that the rents used were gross rents not net rents less operating costs. Using that amended rental information, Ford Baker arrived at a revised market indemnity value of $1,050,000.

[36] That revised valuation was forwarded to the trustees on 1 August 2011. It was accompanied by a copy of the legal advice from Prattley's lawyers and a report from Ms Yates saying:

> I have just forwarded the most recent valuation for Worcester Towers.
>
> We have been having regular meetings with AMP and the insurance Brokers.
>
> At a meeting last week AMP intimated that they realised the valuation they had commissioned was too low and that they might be prepared to settle at $1,050,000 plus GST.
>
> Ray spent quite a lot of time getting our valuation up to the $1,050K but does not believe there is room for any further adjustments.
>
> We said that we would seek approval from the trustees before accepting any offer.
>
> The insured indemnity value was $1,605,000. The policy states that it is payable on a new indemnity valuation and we have checked that this is in fact the legal position in regard to our policy.

[37] The revised Ford Baker valuation obtained by Prattley was also forwarded to Mr Cherry as agreed. On 15 August 2011 he responded to Prattley by email saying:

> In relation to Prattley Enterprises, if it will achieve a settlement, and on a without prejudice basis, I am prepared to settle on the Ford Baker valuation. However, we need to do a bit of work to determine what excess should apply since the excess terms have changed. As at Boxing day, the excess is 5% of the material damage and business interruption sum insured. This is $93,350. But if the building was effectively a total loss in September 2010, then we

> can reduce the excess to 2.5% of the material damage claim ($30,300 by my calculations). It makes quite a big difference.

[38] On 22 August 2011 Mr Cherry forwarded a draft settlement agreement in relation to Worcester Towers. It would pay Prattley $1,050,000 plus GST as per the Ford Baker valuation (a total of $1,207,500), but would be interim only as Vero and Prattley were still to determine what Prattley would be paid for the costs of demolition, the loss of rent, and costs incurred for minor repairs and professional services, and also what excess would be applicable to the claim to be deducted from the amounts owing to Prattley.[2]

[39] That draft agreement was forwarded to Prattley's lawyers who marked up some minor changes, including describing it as an interim settlement agreement to reflect that there were still some matters to be resolved. However, the terms on which the settlement sum for the loss of Worcester Towers was being paid, were expressly stated to be the subject of a binding agreement.

[40] Clause 4 of the Agreement stated:

> Except as noted in 5 below, the Interim Settlement Sum is paid by Vero and accepted by the Insureds in full and final settlement and discharge of the Claim and any claims against Vero arising directly or indirectly out of, or in connection with the Earthquake Activity and/or the Policy and/or the Insured Property Damage whether such claims arise under statute, common law, or equity; are in existence now or may arise sometime in the future; are known or unknown; in the contemplation of the parties or otherwise. This includes the discharge of any further claim under the Policy for damage, loss or other entitlement under the Policy occurring subsequent to the date the Insured Property Damage occurred, whether or not that further claim has been notified to Vero.

[41] Clause 5 simply listed the aspects of the claim that Vero and Prattley were to separately agree, which included the excess applicable to the claim. The Agreement also went on to say "The Insureds acknowledge that they have been advised by Vero to obtain their own legal advice before entering this agreement". In any event, Vero was aware that Prattley had taken legal advice, because the Agreement had been reviewed and marked up by Prattley's solicitors and those changes were incorporated before the Agreement was finalised for signing.

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[2] Given the excess change from 2.5% of the loss to 5% between 2010 and 2011.

[42] The Agreement was signed by Mrs Britten for Prattley on 23 August 2011 at Amicus' office, following the trustees' approval being given. That approval was solicited by circulating the proposed agreement by email to the trustees, who had already received the legal advice from Mr Weir's firm, Anthony Harper, and the valuations from Ford Baker and Knight Frank.

[43] Payment of the settlement sum was received by Prattley on the morning of 25 August 2011.

Prattley reopens the claim

[44] In late 2011, Risk Worldwide New Zealand Limited (Risk Worldwide) was incorporated by individuals from the United States with experience in the insurance industry. Mr Keys, one of the directors of Risk Worldwide, explains that for the last 21 years he has "worked for the insured policy holders in the investigation and presentation of material damage claims to the insurers".

[45] Risk Worldwide, through its website, offered to assist policy holders recover "the missing billions" including by reviewing "settled commercial claims". Prattley entered an agreement with Risk Worldwide in July 2012 to "investigate and prepare the claims arising from earthquake damage to its property at 103-105 Worcester Street, Christchurch".

[46] Risk Worldwide conducted its own assessment of Prattley's claim and submitted a claims package in respect of the damage to Worcester Towers to Vero on 8 May 2013. That claim package sought payment of $8,776,955.75 as set out in a statement of loss. This sum comprised $8,125,216.17 for "building replacement estimate" plus various other associated claims for demolition, business interruption, professional fees and the like and sought payment of that sum "less the excess and previous payments".

[47] Vero rejected the invitation to revisit the sum paid pursuant to the Agreement and these proceedings ensued.

[48] The relief pleaded by Prattley is either damages of $6,518,073.40 including GST (being $7,973,067.53 less $1,207,500 already paid) or, if the "total sum insured" is a prescribed limit for each of Prattley's earthquake damage claims, Prattley claims damages of $2,842,343 (being $4,049,843 less $1,207,500) already paid. However, the hearing has proceeded on the basis that Prattley's claim is limited to $1,605,000 for each event, and so the lesser amount pleaded is sought.

[49] It is fundamental to the claims made by Prattley that it must first establish that its entitlements under the terms of the relevant insurance policies, if correctly interpreted and applied, would exceed the payment received under the Agreement. This involves both a review of the policy terms and then a factual assessment of the value of the claims. I consider the policy first.

The contract of insurance

General

[50] Prattley's entitlement arises under two separate insurance contracts with Vero, one for 2010 and one for 2011. The only material difference between the two contracts is the excess which applies.

[51] The policy document sets out positive obligations on Vero, including to comply with the Fair Insurance Code of the Insurance Council of New Zealand. The policy summarises these obligations as follows:

> This means we will:
>
> 1. provide insurance contracts which are understandable and show the legal rights and obligations of both us and the policy holder;
> 2. explain the meaning of legal or technical words or phrases;
> 3. explain the special meanings of particular words or phrases as they apply in the policy;
> 4. settle all valid claims fairly and promptly;
> 5. clearly explain the reason(s) why a claim has been declined;
> 6. provide policy/holders with a written summary of our complaints procedure as soon as disputes arise and advise them how to lodge a

> complaint and tell them about the Insurance and Savings Ombudsman scheme;
>
> …

[52] The Schedule relating to cover for Material Damage describes the cover type as "Indemnity" and the Material Damage section of the policy explains the scope of the indemnity as follows:

> We will indemnify you for *damage* to any of the *insured property* occurring during the *period of insurance*.
>
> You will be indemnified by payment or, at *our* option, by repair or replacement of the lost or *damaged* property.
>
> Subject to the reinstatement of amount of insurance extension *our* liability will not exceed the total sum insured; or where more than one item is included in the *schedule* will not exceed in respect of each item the sum insured applicable to that item.

[53] Under the heading 'Exclusions' in the Material Damage section, cl 7 provides that earthquake damage is not insured. However the section goes on to provide for various extensions to the cover provided but states they are to have no effect unless "there is a statement in the *schedule* that the particular extension will apply".

[54] The two extensions providing earthquake cover are:

(a) Earthquake indemnity cover MD020; or

(b) Earthquake full reinstatement cover MD022.

[55] The policy schedule for Worcester Towers in respect of the relevant periods of insurance states that natural disaster is insured and the total sum insured is $1,605,000. Vero acknowledges that Prattley had earthquake indemnity cover under MD020 as part of its policy.

[56] Extension MD020 is in the following terms:

> This extension applies to those items of *insured property* that have a company earthquake sum insured shown in the *schedule*.

> In the event of any *insured property* to which this extension applies suffering *earthquake damage* or *volcanic eruption* or *hydrothermal activity damage* during the *period of insurance* we will cover *you* for such *damage*.
>
> Insurance under this extension is subject to the special provisions set out below
>
> …
>
> *"Earthquake damage"* means:
>
> (a) *damage* occurring as a direct result of earthquakes;
>
> ...

[57] The schedules for Prattley's material damage cover in 2010 and 2011 also had the following provision identified as a "special note":

> We will repair or reinstate the building to as reasonably equivalent appearance and capacity using the original design and suitably equivalent materials.

[58] Under the policy, damage caused by each of the earthquakes for which a claim was lodged was a separate insured event requiring Vero to separately indemnify Prattley. Extension MD020 provides:

> …
>
> (b) Claim adjustment
>
> In respect of each *site* at which *insured property* is located each loss or series of losses arising out of one event will be adjusted separately:
>
> …
>
> A series of events arising from any one cause during any period of 72 consecutive hours will be treated as one event for the purpose of applying the excess.

[59] Clause 19 in the Automatic Extensions part of the Material Damage section provides:

> 19 Reinstatement of amount of insurance
>
> In the event of *damage* for which a claim is payable under this material damage section the amount of insurance cancelled by such *damage* will be automatically reinstated from the date of that *damage*.

[60] The policy sets out definitions of specific words particular to the policy. The definition of 'damage' given in the General Definitions section is, "Physical loss or damage unintended and unforeseen by *you*, and not the subject of a policy or section exclusion".

[61] The definition of 'destroyed' contained in MD020 is when the property is, "so *damaged* that the property, by reason only of that *damage*, cannot be repaired".

[62] Having identified the material terms of the policy, there are a number of issues that arise out of them. I discuss each in turn.

Is Prattley entitled to have each claim for earthquake damage separately assessed and adjusted?

[63] The Agreement was reached on the basis of an assessment following February 22 that the building was destroyed and the full extent of the loss was the market value of the building, whether that occurred over one or several claim events.

[64] Since the Agreement was signed, the Supreme Court has issued a decision in *Ridgecrest NZ Ltd v IAG New Zealand Ltd*, confirming that, in a policy where the indemnity value limit is reset after each event, the claims do not merge and the insured is entitled to recover the aggregate of the losses that can be claimed.[3] This is subject to the proviso that the insured should not realise a profit from the policy except to the extent a policy allows recovery on a replacement basis even though it is more than the actual value of the building.[4] This is so even though repairs for the earlier events are unable to be effected before the building is destroyed by the final earthquake.[5]

[65] The terms of the policy make it clear this is an event by event policy and the insured is indemnified for material damage up to the sum insured on each event causing loss. However, it is also subject to the other limit recognised in *QBE Insurance (International) Ltd v Wild South Holdings* (*QBE Insurance*) that

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3 *Ridgecrest NZ Ltd v IAG New Zealand Ltd* [2014] NZSC 117, [2015] 1 NZLR 40 at [62].

4 *QBE Insurance (International) Ltd v Wild South Holdings Ltd* [2014] NZCA 447, [2015] 2 NZLR 24 at [86].

5 *Ridgecrest,* above n 3, at [50(c)].

"[t]he insurer's liability is always limited by the insured's loss".[6] In *Ridgecrest,* in circumstances where a replacement clause in the policy applied, it was recognised that "the total of all claims cannot exceed the replacement cost of the building" which was the measure of the insured's loss in that case.[7] However, *Ridgecrest* does not determine that this is the measure of loss when the policy is an indemnity policy and where the facts suggest there is no intention to replace the building, an issue I return to later.

[66] In the present case, Prattley argues that the parties did not turn their minds to the full implications of this being an event by event policy, except to the extent this may have impacted on the excess to be applied depending on how damage was apportioned between the September earthquake and the later earthquakes. Once the building was damaged beyond repair the focus was on valuing the building in order to quantify the loss sustained.

[67] Prattley says this exercise should now be undertaken as it will demonstrate that its entitlement under the policy will significantly exceed the amount it was paid under the Agreement and therefore support its claim to reopen the Agreement.

What was the measure of indemnity in the policy?

[68] Prattley argues that under the policy, the depreciated replacement cost is the correct basis for assessing the indemnification cover provided by the policy. It says this is both what the policy provides for and, in any event, is the appropriate cover in all the circumstances of Prattley's ownership of Worcester Towers.

[69] The terms of the policy are of course central to this question. As was noted in *Tower Insurance Ltd v Skyward Aviation 2008 Ltd,* "the applicability of the indemnity principle is subject to the wording of the policy under consideration".[8]

[70] Here, Prattley argues that the insurance policy recognised that the cost of reinstatement formed the basis of the indemnity. Prattley points out that both the

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6 At [58].
7 At [62].
8 *Tower Insurance Ltd v Skyward Aviation 2008 Ltd* [2014] NZSC 185, [2015] 1 NZLR 341 at footnote 12.

general indemnity, and the special note to the policy, reflect this. The indemnity promise in the policy was that Prattley would be indemnified "by payment or, at our option, by repair or by replacement of the lost or damaged property" and that promise was only limited by Vero's liability not exceeding the total sum insured.

[71] In recognition of the apparent heritage classification of the building, Vero also specifically requested the following wording to be added to the policy:

> We will repair or reinstate the building to as reasonably equivalent appearance and capacity using the original design and suitably equivalent materials.

[72] This, says Prattley, is important as it involves an unconditional promise to repair or reinstate, albeit on the specified basis, and it expressly agrees that the cost of repair or reinstatement was how the indemnity was to be satisfied and this applies for each insured event. By including these express terms, it necessarily excludes any other measure of indemnity, including indemnity measured by the "economic value of the property".

[73] Prattley says the other policy terms are also consistent with this approach, as other terms of the policy, including the reinstatement of amount of insurance extension, and the terms of MD020, reflect that the focus of the cover is on repairing "damage" to the property and "damage", means "physical loss or damage".

[74] Vero, by contrast, points out that this is an indemnity policy. The cover type for material damage is described as an indemnity, (which was expressly chosen as the insurance cover by Prattley rather than replacement cover). Similarly, in respect of the policy extension to cover earthquakes, Prattley selected earthquake indemnity cover and not earthquake full reinstatement cover.

[75] As an indemnity policy, the classic articulation of the indemnity principle in *Castellain v Preston*, applies:[9]

> … a contract of indemnity … means that the assured, in case of a loss against which the policy has been made, shall be fully indemnified, but shall never be more than fully indemnified. That is the fundamental principle of

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9 *Castellain v Preston* (1883) 11 QBD 380 (CA) at 386 per Brett LJ.

> insurance, and if ever a proposition is brought forward which is at variance with it, that is to say, which either will prevent the assured from obtaining a full indemnity, or which will give to the assured more than a full indemnity, that proposition must certainly be wrong.

[76] Vero points out that the policy provides simply that "we will indemnify you for damage", and it is silent about the basis on which an indemnity payment is to be calculated. For this reason, Vero says the measure of indemnity is left to be determined according to established legal principles as they apply in the circumstances of the claim. Those principles, as affirmed by the Court of Appeal in *New Zealand Fire Service Commission v IBANZ and Vero Insurance Limited*, are that:[10]

> The term "indemnity value" means the depreciated replacement cost of insured property, or its current market value, depending on the nature of the property and the purpose for which it is held by the insured.

[77] Vero says the special note in the policy schedule limiting the manner in which repair or reinstatement may be carried out has no bearing on the selection of the appropriate measure of indemnity. It simply confirms that, where the cost of repair or reinstatement is relevant, that repair or reinstatement need not be exact, but needs only be undertaken with "suitably equivalent materials" to achieve a "reasonably equivalent appearance and capacity".

[78] Vero also says that where an insured intends to reinstate damaged or destroyed property it may be appropriate for indemnity to be calculated on the cost of doing so, particularly where the insured requires the use of that property to carry on its business, but an allowance for betterment resulting from the reinstatement must be made.

[79] However, where reinstatement is not likely to occur, then diminution in market value will usually be more appropriate because the purpose of an indemnity

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[10] *New Zealand Fire Service Commission v IBANZ and Vero Insurance Limited* [2014] NZCA 179, [2014] 3 NZLR 541 at [5].

payment is to indemnify the insured for a loss that has actually been suffered, not to provide a windfall.[11]

[80] The allowance for betterment is commonly measured by either:

(a) depreciation of the insured property at the time of loss; or

(b) the increase in value of the property upon its reinstatement over its value immediately before the loss.

[81] Regardless of whichever method is adopted, Vero says there must be an allowance for betterment in the calculation of the indemnity sum payable, consistent with the indemnity principle.[12]

[82] I accept that, in terms of the policy, the measure of indemnity is not fixed. The policy anticipates that it will normally be the cost of repair or reinstatement less depreciation. However, the policy does not limit indemnity cover to this option. Instead, the explanation in the policy of the indemnity for material damage leaves it in the hands of the insurer as to whether the insured will be indemnified by payment or by repair or replacement of the lost or damaged goods. Such a provision does not mandate that repair or reinstatement will always be how the indemnity is to be satisfied.

[83] Instead, as discussed in *QBE Insurance*, the measure of loss for which the insured is indemnified may depend on the insured's intentions for the property and the reasons for owning it. That is a factual enquiry and must be made in light of the circumstances applying in each claim event. I consider the appropriate measure of Prattley's loss for each claim in subsequent discussion before determining Prattley's entitlement had it not entered the Agreement.

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11 Citing *Reynolds v Phoenix Assurance Co Ltd* [1978] 2 Lloyd's Rep 440 and *Exchange Theatres Limited v Iron Trades Mutual Insurance Co Ltd* [1983] 1 Lloyd's Rep 674 (QB) where the intention of the insureds to reinstate the buildings was a significant factor in the decision of the Courts to award the costs of reinstatement.

12 Discussed in detail in *QBE Insurance*, above n 4 at [77]-[80] and [85]-[86].

Factual findings in relation to Prattley's claims

What damage was sustained in each earthquake event?

[84] A significant part of the hearing was dedicated to technical evidence on the extent of damage caused to the building in each of the three earthquakes. Prattley's position was that significantly more damage was sustained in the September event than was recognised by eye witness accounts, and that the building was only beyond realistic repair after the February event, which, it says, maximises its entitlement to the per event cap of $1,605,000.

[85] The estimates of damage caused in each event came from two sources:

(a) eye witness accounts and photographs of those who inspected the building at the time, including the Eliot Sinclair engineers; and

(b) computer modelling which attempted to calculate, in percentage terms, the damage suffered by the building in each event.

[86] Vero's evidence is based primarily on the eye witness accounts and contemporaneous records of the damage caused to Worcester Towers through the three earthquakes. They rely in particular, on the evidence of Prattley's property manager, Mr Minehan, who was familiar with the building, and Mr Henry, the Eliot Sinclair structural engineer, who had particular expertise in earthquake strengthening of unreinforced masonry buildings.

[87] Vero also called evidence which concluded that estimates of the probable ground shaking at the Worcester Towers site during each earthquake correlated reasonably well with the extent of damage actually observed in each event. That evidence reinforced that the computer modelling relied on by Prattley was, in this case, an unreliable method of apportioning damage suffered by Worcester Towers in each earthquake event.

[88] Vero's experts assessed the repair cost for the September event at $178,000 plus GST, and for the 26 December 2010 event, a further $3,739,000 plus GST (in

addition to repair costs for September). Vero says at this point the building was past the point of reasonable repair, particularly as the building was earthquake prone and it would have been impracticable to complete the repairs without undertaking necessary seismic strengthening work which would have cost approximately $2,100,000. Indeed, Prattley itself took no steps to pursue the possibility of repair of the building following the pessimistic Eliot Sinclair report of 12 January 2011.

[89] Unlike buildings in other earthquake claims, there was a substantial record of the state of Worcester Towers after both the September and December events. Both Mr Minehan and Mr Henry inspected the building after the September and December events and took photographs. As Mr Henry said:

> The purpose of the inspection was to check the building for earthquake damage, to advise Mr Minehan of the significance of any damage, if any repairs were necessary, and whether the building was safe for ongoing public occupancy.

[90] I am satisfied that these inspections were thorough and were aided by the fact that much of the damage was readily visible because at least 60 per cent of the building's interior walls were exposed brick.

[91] I was also impressed with the consistency of the various eye witness accounts as to the extent of damage after both the September and December events and the support they gained from the photographic evidence.

[92] I am satisfied that, with the repeated inspections by engineers from Eliot Sinclair, combined with the practical expertise of Mr Minehan, and the work undertaken by Prattley's builders, Dutch Construction, who came onto site for the purpose of scoping or undertaking repairs five times in September 2010, there was a reliable assessment of the damage after the September event. This provided a practical basis for the development of the repair scope which was presented by Mr Christopher Kahanek, a structural engineer with extensive expertise in completing damage assessments for commercial buildings.

[93] Accordingly, I accept that Mr Kahanek's repair scope, which was priced by Mr Robert Spence, and concluded that the repairs from the September earthquake

totalled $178,000 plus GST, is reliable, and is the most accurate estimate of repair costs that is likely to be available to the Court in circumstances where the building has since been demolished.

[94] Similarly, but with particular deference to the opinion of Mr Henry, I am satisfied that Vero's assessment that the damage caused in the December earthquake involved further repair work costing $3,739,000 plus GST, is reliable. Again, I found Mr Henry to be a careful witness and his assessment was supported by the eye witness accounts of Mr Minehan and Ms Yates. Mr Henry concluded that there was much greater damage during the Boxing Day earthquake and the damage to the building had "substantially increased from what I had observed at my early inspection following the 4 September earthquake".

[95] As Vero said, it is common ground that Worcester Towers was damaged further by the February 2011 earthquake. Mr Minehan estimated that only 60 per cent of the building was still standing, with some of the damage being caused by the neighbouring Christchurch Press building collapsing on the roof of the west wing of Worcester Towers.

[96] At this stage it is common ground that the building would involve a rebuild at a cost of between $6,243,000 including GST and $7,665,610 including GST, which, in either case, well exceeded the $1,605,000 indemnity cap in the policy.

[97] Prattley's evidence in response is to rely on a computer modelling approach presented by Dr Anurag Jain, which produced a different assessment of the proportion of damage suffered by Worcester Towers in each of the three events. His modelling resulted in an apportionment of damage as follows:

> September – 26.1 per cent
>
> October (a small earthquake event for which no insurance claim was made by Prattley) - 0.8 per cent
>
> December – 4 per cent
>
> February – 69.1 per cent

[98] Dr Jain's model seeks to estimate the potential for damage to Worcester Towers in respect of each event by measuring the total energy applied by each earthquake to the mass of the building. The model translates Worcester Towers into what was described as a "single degree of freedom oscillator" which was analogous to a lollipop. The round head of the lollipop represents the mass of the building and it moves on a stick which represents the stiffness and strength of the building. The lollipop moves on a horizontal plane when the estimated force of the earthquake is applied. When the building moves beyond its elastic force-deformation capacity, damage results, and the model is able to estimate the deterioration in the building's ability to withstand subsequent earthquake shaking as it is progressively damaged in the repeated earthquake events.

[99] While Dr Jain argued that the Court could rely on the model to be satisfied as to the percentage of damage caused to Worcester Towers by each of the events, Vero, through its witness Dr Nicholas Brooke, asserted that Dr Jain's model had a number of limitations. Specifically:

(a) the stiffness and strength assumed in the modelling is not an assessment of the properties of Worcester Towers but is a ratio taken from the HAZUS manuals for an average unreinforced masonry mid-rise low code building;

(b) the model makes assumptions about the factor by which the stiffness of the building degrades as a result of each earthquake;

(c) the model assumes that the building is a square and is just as strong in one direction as it is in the other;

(d) the model does not take into account the specific quality of the masonry in the building;

(e) the model does not provide for the asymmetric shape of Worcester Towers;

(f) the model takes no account of the poorly constructed butt joints in the building; and

(g) the model assumes the same seismic mass for the building in both the east-west and the north-south direction;

(h) the model does not account for damage caused by another building collapsing on to it as The Press building did in the February earthquake;

(i) the model does not deal with non-structural items such as the fit-out of the building.

[100] Furthermore, while Dr Jain accepted that it was crucial to the credibility of the model that the results were corroborated by the reality of what was observed, it became clear, in cross-examination, that Dr Jain's understanding of what physical damage was observed was inconsistent with the evidence that had been given at the hearing. That was then rationalised by Dr Jain as the earlier damage being hidden damage which "softened" the building, causing damage which was not visible on inspection.

[101] By comparison, Dr Brooke gave evidence which critiqued the relevance of Dr Jain's modelling to Worcester Towers and explained why, in his view, the most effective means of apportioning loss was to use the available information in the form of eye witness accounts and photographs, in conjunction with engineering judgment. He also undertook a comparison of observed damage with earthquake shaking levels calculated from nearby recording stations and found they correlated well to the damage recorded for each event. He did not accept there was evidence that the building had materially "softened" in the September quake and according to Mr Kahanek, any such softening would be "negligible in effect".

[102] While I accept Dr Jain's modelling will have utility where there is a more conventional building structure and a lack of reliable recorded evidence as to the extent of damage the building suffered in each claim event, I do not consider it assists in the present case. The allocation of damage which the model arrives at as between the three earthquake events is so at odds with the observed damage that I do not think it is a reliable tool to calculate what in fact needed repair after each event.

[103] Furthermore, I do not think the model's percentage allocation of damage to each event can be directly translated to a share of the total repair or reinstatement cost as Prattley has assumed. Costs will not increase in a uniform or linear fashion

depending on the stress the building was placed under. Instead, costs will rise in a non-linear fashion with each earthquake event, as they will depend on whether the damage sustained reaches the threshold where it warrants a cosmetic repair, a major repair, or total replacement of the damaged item.

[104] I therefore found the approach used by Mr Kahanek and priced by Mr Spence, the most reliable way of quantifying the cost of repairing the damage suffered as the result of each earthquake event, and I accept their evidence on those issues.

Was Worcester Towers destroyed in December or February?

[105] The parties differed as to whether the building was destroyed after the December event or after the February event. The significance of this is, of course, that there would be no further claim for the February event if the building was destroyed by the December event.

[106] Vero relies to a large extent on the report of Eliot Sinclair dated 12 January 2011 where Eliot Sinclair's engineers expressed the view that "the building has been so seriously damaged that repair and strengthening of the building is unlikely to be a viable proposition". That view was reiterated by the insurer's loss adjuster who reported in early January 2011 that, after inspecting the building, he believed it would be "uneconomical to repair". Vero therefore says that the extent of the damage, combined with the cost of repair and of earthquake strengthening work (estimated at $2.1 million) meant it was completely uneconomic to repair the building at this stage and the only realistic scenario is to treat the building as destroyed in December.

[107] The concept of when a property is "destroyed" for the purposes of an insurance policy was discussed in *QBE Insurance* but there it was held that the question of whether the insured property has been destroyed is a question of fact to be answered in all the circumstances.[13] While, in most circumstances, a property would be considered to be destroyed when the damage sustained is sufficiently

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[13] *QBE Insurance*, above n 4.

extensive to adopt rebuilding cost as the appropriate measure of loss, that must, as with everything, be subject to the express terms of the policy.

[108] In this case, the policy provides its own definition of 'destroyed', saying it means "so damaged that the property, by reason only of that damage, cannot be repaired". This definition clearly focuses on the feasibility of repair rather than incorporating any measure of economic practicality into that definition.

[109] Thus, while Eliot Sinclair's engineers doubted the economic viability of repair after the Boxing Day earthquake (a conclusion which I found plausible), they concluded it was feasible to repair the building. It was only after the February earthquake, where the building was so damaged that it had to be demolished, that Worcester Towers could be said to have been "destroyed" in terms of the policy definition.

What was Prattley's intention at each claim event?

[110] As has been discussed above, because the policy is one of indemnity, the relevant loss is the loss to the insured and the measure of that loss will depend on the insured's intentions for the property. Thus in *Reynolds v Phoenix*, when a brick malt house was insured for £550,000 under a replacement policy, it was held the cost of repairs following fire damage of £243,000 reflected the true measure of loss, even though an equivalent modern malt house could be built for just under £30,000.[14] In that case, Forbes J found that the insured genuinely meant to reconstruct the building and that desire was not eccentric or unreasonable.

[111] However, where the insured's interest in the damaged property is confined to a commercial use that can equally well be carried on in a functionally equivalent new building, the higher cost of reinstating the original structure was held not to be the true measure of the insured's loss.[15] Futhermore, where the insured intends to sell the building then its market value is obviously the correct measure of the loss.[16]

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14 *Reynolds v Phoenix*, above n 11.
15 *Exchange Theatre Limited v Iron Trades Mutual Insurance Co Ltd,* above n 11.
16 *Leppard v Excess Insurance Co Ltd* [1979] 1 WLR 512 (CA).

[112] There is no real dispute that Prattley's intention following the September earthquake was to repair the building and retain its tenants. That being so, the cost of repair, is the correct measure of its loss at that point in time.[17] It is more difficult to say what Prattley's intentions were after the Boxing Day earthquake, because Prattley had so little time to commit to any particular option before the events of 22 February 2011 overtook it.

[113] There is some evidence to suggest that, even at this stage, Prattley was considering whether to undertake repair work at all. On 19 January 2011, Ms Yates made the first enquiry of Mr Weir, one the lawyer trustees, at the behest of another trustee, Mr Corcoran, as to whether Prattley was obliged to rebuild. She asked Mr Weir; "Being an indemnity policy [Mr Corcoran] wanted to know if Worcester Towers was knocked down as a result of earthquake damage do we get the money or are we obligated in any way to rebuild?"

[114] However, Eliot Sinclair was engaged to assess the damage and to provide preliminary advice on a repair strategy, which it did in its report of 12 January 2011. Furthermore, Prattley's advice to tenants on 14 January 2011 assumed that repair work would be carried out if that was supported by the insurance assessors. Given subsequent advice that a repair option was feasible, albeit that Prattley would have had to meet the significant shortfall between the cap in the insurance policy and the full cost of repairs required at that stage, I consider that Prattley's intention was still to repair the building. Consequently its measure of loss should still be referenced to the further costs of repairs at that stage.

[115] However, following the 22 February 2011 earthquake, when the building had to be demolished because of the extent of the damage, repair was no longer an option. Prattley's only options now were to:

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[17] Noting Vero asserted it did not intend to make any deductions for depreciation from the cost of repairs following this event.

(a) reinstate Worcester Towers, albeit using modern construction methods and equivalent materials at an estimated cost of between approximately $6 million and $8 million including GST;[18]

(b) develop the site in some other way to maximise value on the site; or

(c) sell the land.

[116] Prattley, through Mrs Britten, asserted that Prattley's loss should be based on the depreciated replacement cost of the building, as that was the appropriate measure of loss because:

(a) there was a connection between the Britten motorcycle museum and the site;

(b) Prattley's intention was to rebuild;

(c) location was important to Prattley;

(d) the building was regarded as the home of the Britten motorcycle and the home to the Britten family businesses;

(e) the location was hunted out by fans and provided good access and foot traffic from Cathedral Square; and

(f) Mr and Mrs Britten had an attachment with the site for its heritage values and considered the building "interesting and unique".

[117] However, on the evidence, I am satisfied that the primary purpose of Prattley holding the building was for its income earning potential. Mrs Britten confirmed in evidence that the building was used to generate income to support her family. The concept of doing something else with the site was clearly entertained by Prattley even before demolition, as one of the first questions asked of Prattley's lawyers was

[18] Being the range of prices the quantity surveying experts reached based on the Thornton Tomasetti scope of works for a modern equivalent building, but where Prattley's expert assumed four further elements should be added to the scope of works.

whether Prattley were obligated to rebuild if it was paid out on an indemnity basis. It is also relevant that the trustees chose to insure this building on an indemnity basis, whereas other newer buildings held by them were insured on a replacement basis. Thus they insured on the basis that they would recover the loss of their investment, but not be able to replace the building.

[118] In all the trustee's communications regarding the decisions to be made about the site and the building, their focus was on enhancing value for the benefit of the Britten family. After receiving the settlement payment, the trustees were in communication with a real estate agent who was bringing them offers for the site. However, the view that emerged was that they should not sell until they had talked about what the estate's strategy was going forward, taking into account what they could do under the soon to be released Canterbury Earthquake Recovery Authority plan for the development of the central city. When the plan was released, the view expressed by the trustees was that they would continue to monitor developments as there "will be a use for [the sites owned by the Trust] that will enhance value".

[119] Later on, with the agreement of the trustees, the real estate agent, Harcourts, was provided with an exclusive sale agreement for the site, with a price guide of between $2.2 and $2.5 million, again demonstrating that the trustees were focused on maximising value to the Trust rather than reinstating Worcester Towers.

[120] Most importantly, had Worcester Towers been rebuilt, then the agreed costs to rebuild Worcester Towers, plus the land value of $2 million, would have totalled more than the $7 million value that Mr Stanley, Vero's expert valuer, attributed to the site when redeveloped. Mrs Britten accepted that neither she, nor the other trustees would make a decision that did not make financial sense. On the evidence presented, rebuilding Worcester Towers would not be an economically rational decision, and would not be supported by the trustees.

[121] In short, I am satisfied that given the commercial expertise of the trustees, and the evidence of the decisions that were taken after 22 February 2011, the trustees only intended to make decisions for the site which were financially advantageous for the beneficiaries of the trust. There was no evidence to support the notion that

rebuilding Worcester Towers was entertained at all. Instead, the site was looked at consistently in terms of what was the most profitable option for its use. Those options included selling it at a profit and investing in other better located properties, or waiting to see what could be done on the site under the new city plan and developing the site in a way that maximised its potential under that new planning framework.

[122] In respect of the connection of the Britten family with that site as the "home of the Britten motorcycle and to the Britten family businesses", that may have been the case, but it had no bearing on the future use of the site and was contradicted by the trustees' willingness to sell and invest in better located land.

[123] Similarly, any attachment that the Britten family had to this "quirky" old building was, of course, severed when the building had to be destroyed. There was no evidence that a modern replica would generate the same sense of attachment, and in any event, it was not something which the trustees would have allowed to take precedence over making prudent investment decisions.

[124] For all these reasons, I do not consider that, when Worcester Towers was destroyed on 22 February 2011, the appropriate measure of Prattley's loss was the cost of replacing that building.

In light of the policy terms and my factual findings, what was Prattley's entitlement?

Is the correct measure of the insured's loss market value or depreciated replacement cost in the February event?

[125] I have concluded that, contrary to Prattley's assertion, the policy does not confine indemnity cover to depreciated replacement cost, but allows the insurer to elect how the insured should be indemnified, whether that is by a payment of a sum of money, or by undertaking repairs or reinstatement. Thus I do not accept that the policy is only understood to cover the insured for physical damage and for the cost of repair and reinstatement. There is no prohibition on assessing the loss as being the market value of the building in circumstances where the building is destroyed and the insured's intention is not to rebuild.

[126] For the same reasons as I have held that the plaintiff would not have rebuilt Worcester Towers, I consider that, on the loss of the building following the 22 February 2011 event, the proper measure of the plaintiff's loss is the market value of the building. These reasons include that the property was acquired as an investment property to generate rental income for the benefit of the Britten family and, it was insured on an indemnity basis rather than for full replacement.

[127] No steps were taken in 2011 to plan for rebuilding the original building and, even following the December 2010 event, there were enquiries as to whether Prattley would be forced to rebuild in order to get the benefit of the insurance payment. The sale of the site was actively pursued with it being marketed through Harcourts in 2012.

[128] The trustees' objective is to get the best financial outcome for the beneficiaries of the estate. The only trustee who gave evidence and was cross-examined, Mrs Britten, accepted that if rebuilding Worcester Towers was going to cost more than the property would then be worth, the trustees would not sensibly make that decision.

[129] Furthermore, Mrs Britten acknowledged that the Britten Group of companies was in a financial position to proceed with rebuilding if they wished to do so and the fact they have not taken steps towards rebuilding reinforces that replacement of that particular building was not an outcome which the trustees would pursue. I accept therefore that the appropriate measure of indemnity in this case is market value, not depreciated replacement cost.

Calculation of depreciated replacement cost

[130] Although I have found that market value was both an available measure of loss under the policy and was an appropriate measure of loss in all the circumstances, there was a dispute over how depreciated replacement costs should be calculated if that was the measure of loss adopted at 22 February 2011. Specifically, there was a stark difference between the approach taken by the local valuers who had valued Worcester Towers (being Knight Frank and Ford Baker during the course of the negotiations, and Mr Stanley of Telfer Young, who gave evidence for Vero during

the hearing) and Mr Keys, who gave evidence of how he values material damage insurance claims involving damaged property, with particular emphasis on his experience in the United States.

[131] The local valuers applied a single depreciation rate to the whole of the building. The Ford Baker valuations adopted a depreciation rate of 85 per cent and the Knight Frank valuation used a depreciation rate of 65 per cent. Mr Stanley, the expert valuer who gave evidence, applied a 78 per cent depreciation rate to the building based on his estimate that the "economic life" of the building was 112 years and that by 2010 the building had a remaining life of 25 years.

[132] The calculations of depreciated replacement cost undertaken by the local valuers ranged from $700,000 to $1,400,000. In contrast, Mr Keys' evidence used an "elemental approach" which depreciated different parts of the building at different rates, but with many of the internal components (for example, plumbing and structural walls) not being depreciated at all and other components (such as doors and ceiling linings) being depreciated at a rate of only 10 per cent. Overall, the depreciation percentages applied by Mr Keys equated to an overall depreciation rate for Worcester Towers of about 10 per cent, meaning its depreciated replacement cost would be around 90 per cent of the new build cost.

[133] Given my findings as to the appropriate method of calculating Prattley's loss, I do not need to discuss, in any detail, the differences between the approach of Mr Keys, and the local valuers. However, I observe that the approach used by Mr Stanley is an orthodox approach mandated by the International Valuation Standards and New Zealand valuation practice. The Australian and New Zealand Valuation Guidance Note 13 does not provide support for an elemental approach to depreciation as it consistently refers to the physical life of an asset not of its component parts.

[134] I also record that I placed little, if any, reliance on Mr Keys' assessment of the appropriate depreciation rate to apply to the individual items. No clear rationale was articulated for the adopted depreciation rate for each element (whether 0 per cent, 10 per cent, 25 per cent or 50 per cent). In the absence of a clear and full

explanation of the evidence and assumptions that were relied on to support each depreciation rate adopted, I did not find his evidence about the depreciation rate to be applied to each of the various elements of the building either reliable or helpful.

What was Prattley's entitlement under the policy?

[135] It is critical to Prattley's claim that it was entitled to more under the policy than the sum of $1,200,000 (GST included) for the material damage to Worcester Towers. Prattley argues that it was entitled to be paid on the basis that it intended to replace Worcester Towers and therefore that the approach in *Ridgecrest* applies, where the successive claims for loss in each earthquake event can be aggregated, as long as they do not exceed the cost of replacement of the building.

[136] However, I have found that Prattley did not intend to replace the building following the 22 February 2011 event. Thus, while I accept that Prattley Enterprises is entitled to make a claim for each earthquake event, I need to consider how the indemnity principle applies in successive claims, where I am satisfied there was no intention to rebuild Worcester Towers.

[137] The indemnity principle is a principle that is said to pervade all indemnity contracts: the insured cannot recover more than its loss under the policy, or the insured cannot make a profit.[19] Put in another way, an insured cannot claim for a loss that it does not incur. The Supreme Court in *Ridgecrest* dealt with the indemnity principle in the context of the successive claims for both indemnity and replacement cover, albeit subject to a cap. The Court accepted that the indemnity principle would preclude recovery of more than the replacement value of the insured property, and Ridgecrest NZ Ltd was not seeking to recover more than the replacement value anyway.

[138] The Court of Appeal in *QBE Insurance* dealt with the indemnity principle in an indemnity cover only context (albeit where reinstatement was intended) and is

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19 *Ridgecrest,* above n 3.

more relevant to Prattley.[20] It confirmed in clear terms that the indemnity principle survives *Ridgecrest*.

[139] The following statement by the Court of Appeal is relevant here:

> [86] It is true, as Mr Kennedy argued, that when event #1 happened the insurer became liable in contract to indemnify the insured for the resulting loss and the insured acquired a corresponding cause of action. He complained that the insurer wishes to deny the insured its right to indemnity for the unrepaired damage from event #1. This argument assumes that the policy ought to have legislated for every contingency. *In fact the damage was overtaken by event #2 before it could be repaired* and it is likely that the cost of repairing the accumulated damage is likely to be less than the cost of repairing each loss separately. Indeed, it may well be impossible to repair one without the other. Where that is so, *the insured will never actually incur the expense of remedying the unrepaired damage* from event #1. *To recover expenses that the insured will not incur in addition to its actual expenses of remedying the accumulated damage after event #2 is to realise a profit from the policy*, a result probably not intended in a contract of indemnity. (emphasis added)

[140] This illustrates that where an insured will not actually incur the costs of repair, such costs cannot be recovered because they do not represent loss to the insured.

[141] The Court went on to give two more examples:

> [87] In the example given in [56] above, we assumed that the cover cancelled by loss upon event #1 was $3m and the sum insured of $8m was available for a future event #2.
>
> [88] Now suppose that later in the policy term event #2 happens, causing additional loss of $7m, again in the form of reinstatement costs. *Assume the unrepaired loss from the accumulated damage is $9m, somewhat less than would be the case if separately remedied. That sum is the insured's actual loss;* it is the amount that the insured will spend to reinstate the property to the policy standard. The insured may claim that sum notwithstanding that it exceeds the sum insured of $8m, because the amount claimed results from two events the loss from each of which was less than the sum insured. The amount claimed is also less than the total replacement value of the property, $12m.
>
> [89] Suppose next that the *insured had already incurred expenses of $1m for repairs* when event #2 happened. *In that case the insured's actual loss is $10m, comprising the cost of reinstatement after event #2 and the $1m already incurred for event #1*. That too is recoverable for the reasons just

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[20] *QBE Insurance*, above n 4.

given, but subject of course to any other policy limits.
(emphasis added)

[142] Despite the event-by-event basis of the insurance contract, the basic principles of insurance law remain and hold that an insured cannot recover for loss that has not been, and will not be, incurred.

[143] In the Prattley context the same approach applies, but it leads to a different result being that Prattley can recover only the market value of the building. I reach this conclusion because, although damage was incurred in each event, no substantial repairs had been carried out. At the third event the building was destroyed so the cost of repair was overtaken by the costs which represented Prattley's loss at that point. As I have found that Prattley did not intend to rebuild, I consider that the loss to Prattley at this point was the value of the building.

[144] The damage in the first two events cannot be regarded in a vacuum simply because the policy was on an event-by-event basis. Under both *Ridgecrest* and *QBE Insurance,* the measure of the insured's entitlement is still referenced to the loss that has actually been suffered. If Prattley is paid for each event, it would be receiving money for repairs that had not been, and now could not be, carried out, that is, loss which it had not suffered. It is clear from the Court of Appeal's decision in *QBE Insurance* that that is not the correct result.

[145] While it might seem unusual that the claim following the third event is a lesser entitlement than the claim following the second event, that is because the effect of the third event is to reduce Prattley's loss.

[146] To provide a simpler example, if a brick wall was damaged in one event, it might be expensive to repair because such repairs are labour intensive. If it was completely destroyed in a subsequent event so that repair was made impossible, it may be cheaper to install a modern equivalent wall if that is permitted by the policy's terms. In those circumstances, the cost of the cheaper option, which becomes available because the wall has been destroyed, would be the maximum measure of the plaintiff's loss.

[147] The situation would have been different for Prattley if I had accepted that a rebuild of Worcester Towers was going to take place. In that case, following *QBE Insurance* and *Ridgecrest*, it would depend on the cost of repair and, as I have found, it would total $178,000 for the first event, $1,605,000 for the second event and, in all likelihood, $1,605,000 for the 22 February event, being a total of approximately $3,400,000. That is less than either the insurer's rebuild cost of $5,429,000 plus GST on the insured's rebuild cost which is significantly higher. This would allow for the separate events, so reflecting the event-by-event nature of the policy, without exceeding the actual costs of a rebuild and thus would reflect the indemnity principle.

[148] Accordingly, I have found that Prattley was entitled to the market value of Worcester Towers after the third event, and payment of that sum properly compensated Prattley for its losses, because it never would incur the losses of the repairs following the first two events. The Ford Baker valuation used for the Agreement was not a reliable assessment of market value because it relied on erroneous information about rental yields which favoured Prattley. The evidence of Mr Stanley arrived at a market value of $520,000 for Worcester Towers prior to the earthquake damage. That seems a realistic figure and was not challenged in any substantive way by Prattley. However, I need make no final finding on the market value of Worcester Towers except to say it was less than the sum paid to Prattley under the Agreement.

[149] That finding, of course, means that, strictly speaking, I do not have to consider the issues regarding the validity of the Agreement. However, for completeness, I go on to do so.

Setting aside the Agreement

[150] The second major limb to Prattley's argument was that, as its entitlement under the policy was greater than it received under the Agreement, the Agreement should not be enforced for the following four reasons:

(a) The Agreement was the consequence of Vero breaching its obligations under the policy of good faith and fairness in dealing with Prattley in

relation to the settlement of Prattley's claims. The key breaches were that Vero wrongly advised Prattley its entitlement was limited to market value of the building prior to the earthquakes and did not assess the damage on a per event basis.

(b) In any event, the Agreement is not enforceable as a true contract of compromise as it is not supported by consideration.

(c) The Contractual Mistakes Act 1977 applies as Prattley was mistaken as to its entitlement under the insurance policy and Vero either knew Prattley was mistaken or was mistaken itself about those entitlements.

(d) The same conduct amounted to misleading and deceptive conduct in trade under the Fair Trading Act 1986. Whether intentionally or otherwise, Vero misrepresented what Prattley's entitlement was to Prattley and such statements cannot be regarded as mere opinions or as advice which it was unreasonable for Prattley to rely on.

[151] Even though I have held that Prattley did not have an entitlement which exceeded the payment under the Agreement, I have gone on to consider these arguments, in the event my finding as to entitlement is successfully challenged.

Did Vero breach its contractual obligations to Prattley?

The alleged breaches

[152] Prattley argued that Vero had both express and implied obligations to act fairly in the settlement of claims, and Vero's obligation to act fairly was defined both in the contract, and imported through Vero's obligation to comply with the Fair Insurance Code.

[153] In particular, Prattley relies on the fact the Code provides:

> When you make a claim, we will:
>
> - explain how to report your claim

- explain what information you must give us to process your claim
- explain the steps we will take while handling your claim
- tell you that the information you give us must be honest, complete, up to date and relevant
- keep you informed of the progress of your claim
- settle all valid claims quickly and fairly
- clearly explain how we reached our decision
- clearly explain the reason if your claim is declined.

[154] In alleging that Vero breached these obligations, Prattley says the key failure was that it incorrectly represented what Prattley's entitlements were, and then secured a settlement on that basis.

[155] Prattley argues that, under the policy, its entitlement to damages was the cost to repair the damage, subject to any deduction for depreciation, so in giving the advice that the measure was market value only, Vero was in breach of the policy by failing to explain the proper measure of indemnity. It is also argued that Vero breached the policy by failing to explain that damage needed to be apportioned and measured on a per event basis, and, by simply adopting market value as the combined loss in all three claims, Vero failed to do this.

[156] Prattley asserts that Vero recognised the "per event" nature of the policy, and its importance when assessing the entitlements but did not disclose this. When Mr Cherry received the second loss adjuster's report on 4 February 2011 enclosing the Eliot Sinclair report, he appreciated he needed to understand how the damage should be apportioned between the September and December events because of the terms of the policy, and he set reserves accordingly. As a consequence, on 7 March 2011 the reserves were adjusted to a total of $2,100,000 GST inclusive because Vero understood that Prattley's claim was not capped at the total sum insured, because of the "per event" character of the policy.

[157] Although Mr Cherry had set reserves on an event by event basis, Prattley says that at the 14 June meeting, Mr Cherry did not disclose Vero's internal view that

the damage needed to be apportioned per event. Rather, the discussion focused on assessing the indemnity value, which Mr Cherry had said was market value and in relation to which he would obtain a valuation. From that point onwards, engineering input was no longer sought in order to apportion damage per event, and the parties focused solely on the pre-earthquake market value of Worcester Towers with the focus being on the competing Knight Frank valuation and Ford Baker valuation.

[158] Similarly, in the second meeting on 15 July, the insurer again confirmed that Prattley's entitlement was to the market value of the building. As a consequence, the parties focused on agreeing the market value, which eventually they did, adopting the second Ford Baker valuation for settlement of the claim in the Agreement.

[159] Finally, Prattley submits that even if the Court determines that market value may be an appropriate measure of loss under the policy in some cases, Vero failed to make the appropriate inquiries about Prattley's loss which would have revealed that depreciated replacement cost was the appropriate measure of loss in this case. That is because of the matters set out above, including that Prattley's intention was to rebuild and that the Britten family had a particular attachment to the site and to the building which they considered interesting and unique.

[160] Prattley also says that the involvement of Prattley's lawyers in giving advice about indemnity value was irrelevant because Prattley asked Vero what the entitlement was and did so before it received legal advice.

[161] Accordingly, Prattley relies on the principle of law that a party shall never take advantage of his own wrong,[21] and says that Mr Cherry's advice was wrong and misled Prattley into accepting a disadvantageous amount to settle its claim. Vero should not therefore be entitled to rely on the Agreement to deny Prattley its full entitlement under the policy.

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[21] See *Rede v Farr* (1817) 6 M. & S. 121 at 124; *Doe d. Bryan v Bancks* (1821) 4 B. & Ald. 401 at 409; *Total Transport Corp v Amoco Trading Co* [1985] 1 Lloyd's Rep. 423 at 426.

Vero's response

[162] Vero did not contest that it had an obligation to act fairly, to explain the meaning of indemnity, how it applied and then to settle the claim fairly and promptly. Vero also accepts that it has made a commitment to comply with the Fair Insurance Code.

[163] However, Vero says that nothing in these terms can be read as imposing on Vero an obligation to give advice to Prattley about the meaning of a promise to indemnify Prattley for its losses, in circumstances where Vero knew Prattley was taking its own legal advice and Vero had expressly encouraged Prattley to do so. Furthermore, Vero says it is not a breach of any of the pleaded terms for Vero to express a view about policy entitlements, even if that view is subsequently held to be wrong, as it is not a breach of an obligation of good faith or fairness and openness to express a genuinely held view, even if it is mistaken.

[164] Importantly, Vero says Prattley's claim assumes that its entitlement under the policy was "a matter of objectively verifiable fact" capable of "actual proof". Vero says this cannot be the case because:

(a) determining the appropriate measure of indemnity in a particular case is a mixed question of law and fact;

(b) Prattley was as well placed as Vero to seek advice on relevant legal issues;

(c) all the relevant facts were within Prattley's knowledge. It is not a case in which it can be suggested that Vero knew a relevant fact that Prattley did not know, and which Vero should have disclosed but failed to disclosed; and

(d) Prattley's entitlement involves matters of opinion on which reasonable people can and do reach different views. Thus, even if the view expressed was wrong, expressing that view would not be a breach of

an obligation of good faith or of an obligation to deal fairly and openly with the insured.

Discussion

[165] I start by observing that merely because there is a subsequent determination that an insurer's calculation of entitlement is wrong, that does not mean that the provisions of the policy, nor of the Fair Insurance Code, have been breached. If the insurer has been open with the insured, explaining what the terms of the policy mean and how it has gone about calculating the entitlement, then in most circumstances it will have discharged its obligation to act fairly.

[166] In this case, I accept Vero's submission that Mr Cherry dealt with Prattley openly and frankly. In particular, his email of 13 July 2011 sent to Prattley's insurance broker, was a helpful and transparent explanation of the options for calculating indemnity value and of his reasons for thinking market value was the appropriate measure of loss. He says that where the property is repaired, an insured's entitlement "involves the actual cost of repairs less an appropriate allowance for betterment". However, he goes on to explain that the typical outcome when the property is destroyed, as has happened here, is the market value, which he says is because the property owner still has "the land and cash equivalent to investing (sic) in a similar property elsewhere yielding the same returns".

[167] Furthermore, the valuation he provided from Knight Frank prior to this email gave both a depreciated replacement cost valuation and a market based valuation of Worcester Towers, making it obvious both were methods for calculating the indemnity value of the building. Indeed, that is what prompted the enquiry on Prattley's behalf as to which method of settlement would be applied in this case.

[168] Accordingly, I do not consider that there was any breach by Vero in this regard. Mr Cherry made it clear that there were different approaches to indemnity value and he sought and provided a valuation that used both approaches. He also explained why the market value approach seemed appropriate to him in this case. Furthermore, given the information he had, including the commercial tenancy of the building and it being part of a suite of commercial buildings which were held by

professional trustees and managed by experienced staff to provide income for beneficiaries, his opinion was unsurprising.

[169] Importantly, it was sufficient information to allow Prattley to take issue with either the reasoning process adopted, or Prattley's entitlement calculated using that process, which is exactly what Prattley then did through its own valuers and lawyers.

[170] I also accept Mr Cherry's evidence that he never said that Vero would not pay more than market value nor that he had made a fixed decision on the measure of indemnity. That is inconsistent with the way he handled the claim. Rather, once he had explained his view that market value was their entitlement (while referring to the alternative of depreciated replacement cost), the discussion simply moved to pragmatic negotiations on dollar value amount. That was entirely predictable when Prattley's own lawyers had said its loss was the value of the building before it was destroyed.

[171] Mr Cherry's impression that Prattley's representatives wanted to settle on whatever basis would be most favourable to them, and that it was the amount payable that was their focus rather than methodology, was also entirely consistent with the work they were doing behind the scenes. For example, they had already commissioned a market valuation of the building in early 2011 which, I am satisfied from Ms Yates' email of 13 January 2011, was to support their insurance claim. This was well before Mr Cherry was involved. It was reasonable for him to assume that they were not relying on him to inform them of their entitlements under the policy when he knew they were conferring with their own valuers, lawyers and engineers.

[172] The second claimed breach is that Vero failed to explain the need for damage to be apportioned and measured on a per event basis. While Vero recognised it had to apportion the loss over the three separate claims (that was relevant because the amount of the excess changed between the 2010 and 2011 policy), it did not consider whether, as in *Ridgecrest*, there could be an aggregation of the claims for separate damage which could amount to more than the limit on the sum insured.

[173] However, Vero's understanding of the relevance of the "per event" approach when the building was eventually totally destroyed was common understanding at the time, noting it was also the view shared by Prattley's lawyers.[22] Mr Cherry's view was that, where a property was written off before it was repaired, the combined policy entitlements would not exceed the market value of the undamaged building when the building was insured on an indemnity basis. Once it was clear Worcester Towers was beyond repair, the parties abandoned investigation of the scope and cost of repairs for each successive event. However, the need to undertake such calculations was discussed with Mr Minehan in relation to another Britten Group building at 116 Worcester Street, which was being repaired and where it was accepted that the combined claims could exceed the per event limit.

[174] I therefore accept it was not a proposition that was hidden from Prattley and it was averted to in the discussions with the Britten Group representatives. However, at the time, neither the insured or the insurer was of the opinion that, in a total loss situation, the combined entitlements under the successive claims would exceed the indemnity value of the building.

[175] Thus, again the insurer did not act unfairly towards Prattley. Mr Cherry never lost sight of the fact that there were multiple claims, indeed he offered to "weight" the claim to the earlier events to minimise the excess paid. The fact he expressed the view that Prattley's combined entitlement under the three claims could not exceed the market value of the building was simply an expression of his opinion which Prattley's own lawyers also held, but which had the Prattley representatives chosen to challenge, they could have.

[176] Vero also argues a more fundamental defence to this head of claim. It says, even if there had been a breach of the policy terms by erroneously describing Prattley's entitlements, the decision to enter the Agreement was made by the trustees who, apart from Mrs Britten, were not privy to the discussions with Mr Cherry. The trustees simply relied on the legal advice they obtained from their own insurers as to

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[22] It was also the issue debated in some length before the Court in *QBE Insurance International*, above n 4 as outlined at [69]-[89] but in particular at [85]-[86].

Prattley's entitlements under the policy as well as the advice from Prattley's staff that the valuation was the highest that they could obtain.

[177] As Vero points out, no evidence has been given that the three other legally qualified and commercially experienced trustees were relying on Vero to explain how the policy worked and what Prattley's entitlements were under it. No reports they received from Prattley employees ever referred to the statements made by Mr Cherry.

[178] Put simply, three of the four trustees clearly did not look to Vero to explain Prattley's entitlement. The only information they acted on in respect of entitlements was the Ford Baker valuation commissioned by Prattley and the advice from Prattley's lawyers. Equally, while Mrs Britten did attend meetings with Mr Cherry, she did not rely on him. She, too, took advice on these matters and she confirmed in cross-examination that she relied on her fellow trustees and on Prattley's lawyers in deciding to settle on the terms of the Agreement.

[179] Accordingly, even if I considered Mr Cherry had breached any contractual obligation by expressing the opinions he did, I am satisfied that Vero has demonstrated that any loss suffered by Prattley was not as a consequence of relying on what Mr Cherry said, but rather on their own and their advisers' expertise and advice.

Was there a breach of the Fair Trading Act?

The alleged breaches

[180] The alleged breaches of the Fair Trading Act 1986 are, again, that Vero told Prattley that its entitlement was limited to the market value of the building before the earthquakes when that was not true and it did not explain the impact of the "per event" terms of the policy, and how each event was to be assessed separately.

[181] Prattley emphasises that to be liable under that Act, it is not necessary to show that the defendant had any intention to mislead or deceive, simply that the behaviour was misleading or deceptive.

[182] Prattley also relies on the Supreme Court decision in *Red Eagle Corporation Ltd v Ellis*, which emphasised the importance of the context in which alleged misrepresentations were made.[23] In this case, Prattley argues it includes the positive obligations Vero had under the contract of insurance to explain the special meanings of particular words or phrases as they apply in the policy and to settle claims "fairly and promptly". Prattley says Vero's advice cannot be dismissed as mere statements of opinion. The contractual entitlement was "objectively verifiable", and Vero had an obligation to explain what that was. The incorrect statement that Prattley was only entitled to market value therefore amounted to misleading conduct under s 9 of the Fair Trading Act.

Vero's response

[183] The response by Vero is that it is not liable because:

(a) what it said to Prattley was no more than the expressions of opinion which do not give rise to liability under the Act; and

(b) it was not reasonable for Prattley to rely on those opinions.

Discussion

[184] The orthodox view is that a statement of opinion that is made in good faith cannot found a claim under s 9.[24] The statements relied on by Prattley are, in my view, statements of opinion, not of past or present fact. Mr Cherry advised that where a building is destroyed, market value is "typically" the outcome as that allowed reinvestment in a similar building yielding "the same returns". That is clearly a statement of opinion which explains his reasoning and the only past or present fact it relies on is that Worcester Towers was a commercial building held for its investment return, an assumption which was not challenged by Prattley and which I have found to be correct.

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23 *Red Eagle Corporation Ltd v Ellis* [2010] NZSC 20, [2010] 2 NZLR 492.
24 *Premium Real Estate Limited v Stevens* [2008] NZCA 82, [2009] 1 NZLR 148 at [51].

[185] The subsequent discussions Mr Cherry had with Prattley's representatives in July 2011, where he acknowledges that he said Vero considered Prattley was entitled to market value under the policy, was simply an extension of that opinion and, again, did not involve any misleading representation of past or present fact.

[186] As was said in *Premium Real Estate Ltd v Stevens*:[25]

> A person may, in trade, express an opinion that is honestly held and reasonably based at the time it is expressed or relied upon but which subsequent events show to be wrong. In this respect, an expression of opinion may be unlike a misrepresentation of fact, which will be capable of being shown to be wrong at the time it is made. It is difficult to see why an honestly held, reasonably based opinion should be actionable under s 9 simply because it is not borne out by subsequent events. … Accordingly, we consider that there is a fundamental difference between asserting a present fact and expressing an opinion, at least in the present context.

[187] In the present case Vero made it clear that there was not a single method of calculating indemnity value. As a result, its subsequent assertions that it considered market value applied could only be read as Vero's opinion on the option to apply in the present case. That is not misleading or deceptive conduct.

[188] This conclusion is reinforced by the following discussion of the Supreme Court in *Red Eagle* on whether a breach of s 9 has occurred:[26]

> Naturally that will depend upon the context, including the characteristics of the person or persons said to be affected. Conduct towards a sophisticated businessman may, for instance, be less likely to be objectively regarded as capable of misleading or deceiving such a person than similar conduct directed towards a consumer or, to take an extreme case, towards an individual known by the defendant to have intellectual difficulties. ... The question to be answered in relation to s 9 in a case of this kind is accordingly whether a reasonable person in the claimant's situation – that is, with the characteristics known to the defendant or of which the defendant ought to have been aware – would likely have been misled or deceived.

[189] Prattley's representatives at the meetings with Mr Cherry were not unsophisticated people. They included Prattley's insurance broker, Prattley's property manager Mr Minehan (who was negotiating other insurance claims for the Britten Group of companies and for his own companies), and Ms Yates, the professional administrator for the Britten Group of companies. These were people

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25 At [54].

26 *Red Eagle Corporation*, above n 23 at [28].

who undertook their own due diligence on all aspects of the negotiation, including obtaining their own valuation of the building prior to any discussions with Mr Cherry, checking their entitlement under the insurance policy with their lawyers and negotiating a significantly increased market valuation over that provided by the insurer.

[190] Allied to the above point as to whether, in fact, the statements as to entitlement were misleading or deceptive, is the issue of whether Prattley did actually rely on what Vero had told it.

[191] Prattley argues that, as Vero had the "contractual obligation to explain what the position under the policy was", it was "untenable to say that Prattley did not rely on the answers or that it was unreasonable for Prattley to rely on the answers". Prattley says if Vero had in fact advised that it was entitled to repair and replacement costs with an allowance for any depreciation, and that each event was separately assessed, then Prattley would not have settled on the basis of market value and signed the Agreement.

[192] In response, Vero argues that even if a breach of s 9 is proved, the Court must then look to s 43 of the Fair Trading Act and consider whether the claimant has proved that it has suffered loss or damage "by the conduct of the defendant".[27] Here, Prattley argues that there was no reliance, in fact, because Prattley was advised to, and did take its own advice on the issue. That rendered reliance on Vero's views about entitlements under the policy unreasonable both in law and in fact.

[193] As already discussed, I accept that it was neither reasonable for Prattley to rely on Mr Cherry's statements of opinion in these circumstances, nor did Prattley actually rely on them. His statements were not communicated to three of the four decision-makers. Instead, they only received Prattley's own legal advice and Mrs Britten also acknowledged she relied on Prattley's advisers before making her decision.

[194] Accordingly, the claim under s 9 of the Fair Trading Act fails.

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[27] *Red Eagle Corporation Ltd v Ellis,* above n 23 at [29].

Can the Agreement be set aside under the Contractual Mistakes Act 1977?

The alleged mistakes

[195] Prattley's next ground for setting aside the Agreement relies on the provisions of the Contractual Mistakes Act 1977. Section 6 of that Act provides:

> **6 Relief may be granted where mistake by one party is known to opposing party or is common or mutual**
>
> (1) A Court may in the course of any proceedings or on application made for the purpose grant relief under section 7 of this Act to any party to a contract—
>
> (a) if in entering into that contract—
>
> (i) that party was influenced in his decision to enter into the contract by a mistake that was material to him, and the existence of the mistake was known to the other party or one or more of the other parties to the contract (not being a party or parties having substantially the same interest under the contract as the party seeking relief); or
>
> (ii) all the parties to the contract were influenced in their respective decisions to enter into the contract by the same mistake; or
>
> (iii) that party and at least one other party (not being a party having substantially the same interest under the contract as the party seeking relief) were each influenced in their respective decisions to enter into the contract by a different mistake about the same matter of fact or of law; and
>
> (b) the mistake or mistakes, as the case may be, resulted at the time of the contract—
>
> (i) in a substantially unequal exchange of values; or
>
> (ii) in the conferment of a benefit, or in the imposition or inclusion of an obligation, which was, in all the circumstances, a benefit or obligation substantially disproportionate to the consideration therefore; and
>
> (c) where the contract expressly or by implication makes provision for the risk of mistakes, the party seeking relief or the party through or under whom relief is sought, as the case may require, is not obliged by a term of the contract to assume the risk that his belief about the matter in question might be mistaken.
>
> (2) For the purposes of an application for relief under section 7 of this Act in respect of any contract,—

(a) a mistake, in relation to that contract, does not include a mistake in its interpretation:

(b) the decision of a party to that contract to enter into it is not made under the influence of a mistake if, before he enters into it and at a time when he can elect not to enter into it, he becomes aware of the mistake but elects to enter into the contract notwithstanding the mistake.

[196] In advancing this argument, Prattley asserts that it was influenced to enter the Agreement because:

(a) it mistakenly believed that its entitlement under the insurance contract was limited to the market value of the property;

(b) that was wrong because its correct entitlement was to the repair or replacement cost of the building, subject to any depreciation, with each event causing damage assessed separately under the policy;

(c) Vero either also believed that Prattley's entitlement was limited to the market value of the building (a common mistake under s 6(1)(a)(ii)), or alternatively, Vero knew that it was not, or might not be, and knew that Prattley was unaware of this (knowledge of Prattley's mistake under s6(1)(a)(i)).

Was there a qualifying mistake?

[197] Of course, I have held there was no mistake regarding Prattley's entitlement, but, if I assume there was, I do not accept that this was a mistake which fell within s 6(1)(a)(i) of the Contractual Mistakes Act. As Mr Cherry said in evidence "[m]y view was that in the circumstances their loss was appropriately measured by the market value of the building at the time of loss". If that understanding was mistaken then it is a common mistake under s 6(1)(a)(ii).

Was there a substantially unequal exchange of values?

[198] The next element required for a qualifying mistake under the Contractual Mistakes Act is that there be a "substantially unequal exchange of values.[28] Prattley accepts that this involves the exchange of values at the time, not what the rights foregone prove to be worth. Here, the Agreement involved a settlement of claims. Prattley says that this meant that what it was giving away was a claim to seek payment on the basis of depreciated replacement cost, and for a separate assessment of each claim, instead of a claim for market value for the building.

[199] When depreciated replacement costs had been initially assessed by Vero's own valuer at $1,400,000, it is clear that, had Prattley appreciated the possibility of claiming depreciated replacement cost rather than market value, it would almost certainly not have abandoned a claim to argue for that amount by settling for $1,050,000 plus GST.

[200] However, Prattley says its entitlement was significantly greater once the per event approach to losses adopted in Mr Keys' assessment of depreciated replacement cost is used. Furthermore, to abandon a claim in ignorance of its existence involves the surrender of a claim for no value, which must be an unequal exchange of values.

[201] Vero, however, argues that Prattley cannot establish that there was a substantially unequal exchange of values by simply asserting that, had the parties gone to Court, Prattley would receive more than it did under the settlement agreement. Instead the assessment of the exchange of values has to take into account the uncertainties and risks that existed at the time the Agreement was entered into in 2011. Those considerations include the value of the payment received, the value of achieving finality and certainty, of avoiding the cost and delay of an ongoing dispute and, of course, the risk that if market value was adopted, that a significantly lower market value than the one accepted by Vero could have resulted. Vero submits that an enquiry into the relative values exchanged is, in these circumstances "artificial, impracticable and redundant".

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[28] Section 6(1)(b)(i).

[202] I accept that the matter is not as simple as saying Prattley received $1,200,000 for a claim worth approximately $4,000,000. However, Prattley did think it had negotiated the best outcome achievable on a market value-based measure of loss. Had it appreciated there was an alternate method of calculating its loss that was highly likely to have resulted in a higher figure, then I am satisfied it would (as it has now) engaged professionals to assist Prattley to negotiate a higher payment.

[203] Thus, while I accept that the "value" of the Agreement is not simply to be measured in dollar terms but also involves considerations of certainty, avoidance of delay and avoidance of legal costs, it would be artificial to suggest that compromising a claim which, in these proceedings, Prattley says is around $4,000,000 including GST as opposed to a claim which Prattley had valued at $1,200,000 including GST, is not a "substantially unequal exchange of values".

Did the contract allocate the risk of mistake?

[204] Vero argues that s 6(1)(c) of the Contractual Mistakes Act prevents its application because "the contract expressly or by implication makes a provision for the risk of mistakes" of the type argued by Prattley.

[205] Thus, for Vero's argument to be sustained, the Agreement must:

(a) "make provision" for the risk of mistakes; and

(b) oblige Prattley "to assume the risk that its belief about the matter in question might be mistaken".

[206] In the present case Vero relies on clause 4 of the Agreement which provides that the sum was paid:

> … in full and final settlement and discharge of the Claim and any claims against Vero arising directly or indirectly out of, or in connection with the Earthquake Activity and/or the Policy and/or the Insured Property Damage whether such claims arise under statute, common law, or equity; are in existence now or may arise sometime in the future; are known or unknown; in the contemplation of the parties or otherwise.

[207] Prattley argues that this clause in the Agreement was insufficient to meet the requirements of s 6(1)(c) because it does not make any express provision for the risk of mistakes, nor can it be said that it does so implicitly. Prattley says this is a "largely standard clause" and so was unlike the clause in the leading New Zealand authority on mistake, *Shotover Mining Limited v Brownlee*,[29] where the relevant clause was expressly directed to the subject matter of the mistake. Prattley also invoked a statement in the text, *Law of Contract in New Zealand* which states that:[30]

> The principles [relating to s 6] appear to reflect a pragmatic approach which will allow s 6(1)(c) to operate in appropriate cases while preventing it being a shield for undeserving defendants.

[208] However, in the present case, this is a comprehensively drafted provision. It includes any claims:

> arising directly or indirectly out of … the policy and/or the Insured Property Damage … [including] claims [which] … are in existence now … [whether] known or unknown [or] in the contemplation of the parties or otherwise".

[209] The drafting leaves no doubt that the Agreement obliged Prattley to take the risk that it may have an existing, "unknown" claim arising under the policy in relation to the damage to Worcester Towers, which it could be relinquishing. When this is paired with the express recommendation in the Agreement to seek legal advice, which Prattley did, I am satisfied this clause covers the risk that Prattley might be mistaken to the extent of its entitlement under the policy for damage to the property, which is a risk it is prepared to assume, in consideration of the payment being made to it under the Agreement. In other words, this clause expressly covers a claim, such as is now being made, for further or better entitlement under the policy which neither party was aware of at the time of signing the Agreement.

[210] For this reason I am satisfied that the claim of mistake must fail. Prattley accepted the risk of being mistaken as to its entitlement under the policy by the express terms of the Agreement.

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29 *Shotover Mining Limited v Brownlie* HC Invercargill CP96/82, 30 September 1987.

30 Jeremy Finn "Mistake" in John Burrows, Jeremy Finn and Stephen Todd (eds) *Law of Contract in New Zealand* (4th ed, Lexis Nexis, Wellington, 2012) at 352-353.

Absence of consideration for the Agreement

Prattley's arguments

[211] The fourth route by which Prattley challenges the binding nature of the Agreement is that it says the Agreement was not a true agreement of compromise as it was not supported by consideration moving from Vero to Prattley.

[212] Prattley acknowledges that the dispute need only be a "potential" dispute but relies on the text *The Law and Practice of Compromise*, which says:[31]

> … "settlements" of claims made under insurance policies should be seen as forming a category of their own, some of which will have all the characteristics of the compromise of a dispute either as to liability or as to quantum or both, and some of which simply reflect the performance by the insurer of the obligations under the insurance contract.

[213] Prattley says that in this case there was no true compromise because Vero agreed to pay Prattley the full amount of its claim, being the amount in the Ford Baker valuation.

[214] In response to Vero's assertion that Prattley's abandonment of any further claims, including "unknown" claims supporting a compromise, Prattley says this is insufficient as there was no dispute or potentiality of a dispute about unknown claims. In particular:

(a) both parties worked from an understanding that the entitlement was market value and provided a valuation and the insurer simply accepted Prattley's higher valuation, which it had paid for, without demur; and

(b) there was no background of dispute or threatened litigation and there was no real element of give and take as on the face of it, Vero did not give anything more than it was already obligated to pay.

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[31] David Foskett (ed) *The Law and Practice of Compromise*: with precedents (7th ed, Thomson Reuters, London, 2010) at [22-18] (footnotes omitted).

[215] Relying on *Bank of Credit and Commerce International SA v Ali*, Prattley says the Court will be slow to infer a surrender of rights or claims which are unknown, particularly where there was a duty on the other party to disclose the "unknown claim".[32] In this case, Vero had a positive duty of disclosure, being to explain the meaning and effect of indemnity value cover provided under MD020 and it cannot rely on consideration in the form of Prattley abandoning an unknown claim if it had a duty to disclose that claim and it did not do so.

[216] Similarly, Prattley relies on a statement in *Introduction to the Law of Contract in New Zealand*, which says that a valid compromise requires that:[33]

(a) the claim on which the action was based was reasonable (that is, not vexatious or frivolous);

(b) he or she honestly believed in the chances of success; and

(c) he or she has not concealed from the defendant any fact that could affect the validity of the claim.

[217] Prattley says that Vero has "concealed" facts that affect the validity of the claim, given its positive obligation to disclose the relevant matters. It also says that the critical consideration is that a contract of compromise requires forbearance to sue and Vero needs to show that Prattley has abandoned the ability to bring proceedings for settling the insurance payout on a different basis. In this case there was no claim being advanced by Prattley which was being compromised, so Prattley has provided no genuine consideration through abandoning its ability to sue for the higher amount, and Vero's offer to pay the higher market value assessment is not consideration for a compromise.

[218] Prattley says it is not the answer that cl 4 of the Agreement, on its face, involved a compromise by Prattley not to make further "unknown" claims. It also says that Vero needs to establish that it genuinely believed it had a claim to pay less

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32 *Bank of Credit and Commerce International SA v Ali* [2002] 1 AC 251.

33 Maree Chetwin, Stephen Graw and Raymond Tiong, *An Introduction to the Law of Contract in New Zealand* (4th ed Thomson Reuters, Wellington 2006) at 5.2.9.

and that it agreed to compromise this whereas, in fact, Vero was simply performing its pre-existing obligation.

[219] Finally, Prattley says that the usual policy reasons underlying the Court's reluctance to set aside arms' length compromise agreements are not present in this case. Here, the Fair Insurance Code evidences a strongly consumer-based approach to the handling of claims by insurers with the object being to enable policy holders to receive their entitlement. To permit the insurer to take an advantage is inconsistent with the expectations of fair dealing which are reinforced by the provisions of the Code. As the agreement is not supported by consideration, Prattley says it is not binding on it.

Vero's response

[220] Vero argues that payment of the sum of $1,200,000 is good consideration for the discharge. It relies on the exception to the rule in *Foakes v Beer*, which says that, while payment of part of a debt is not good consideration for promise to forego the balance of the debt, an exception applies where the claim is for an unliquidated sum, or where the amount owing is in dispute.[34]

[221] As *Chitty on Contracts* puts it.[35]

> … the general rule [in *Foakes v Beer*] applies only if the general claim is a "liquidated" one, i.e. a claim for a fixed sum of money, such as one for money lent or for the agreed price of goods or services. It does not apply where the creditor's claim is an unliquidated one, such as a claim for damages or for a reasonable remuneration (where none is fixed by the contract). The value of such a claim is again uncertain; and even if the overwhelming probability is that it is worth more than the sum paid, the possibility that it may be worth less suffices to satisfy the requirement of consideration.

[222] I accept that this exception applies in this case. Prattley's entitlement under the Agreement was unliquidated, and, even assuming that depreciated replacement value was the correct measure of loss, there was room for legitimate debate about that sum. Prattley obtained the benefit of a promise to pay a specified sum and

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34 *Foakes v Beer* (1884) 9 App. Cas. 605.

35 GH Treitel "Consideration" in HG Beale (ed) *Chitty on Contracts* (31st ed, Thomson Reuters, London 2012) at [3-119].

without the need to engage in dispute resolution procedures or litigation, which would involve cost and delay.[36]

[223] Vero also relies on the principle that there is good consideration to support a settlement agreement between two parties when it is entered into in good faith. In support of that proposition, it cites *Couch v Branch Investments (1969) Ltd*, where McMullin J said:[37]

> … except in those cases where the agreement in respect of which the forbearance to sue is given is a sham, or so frivolous or vexatious that it is patently obvious, even to a layman, that it could not succeed, or so lacking in any foundation as to make its assertion incompatible with both honesty and a reasonable degree of intelligence, or a fraud, the Courts will not enquire into the merits of the cause of action upon which the forbearance to sue is based. It will be sufficient if the promisee honestly believes that he has a good cause of action.

[224] Vero emphasised that the courts will insist on a high threshold being reached before going behind a compromise because of public policy reasons including encouraging settlement and the advantages to litigants of settling these disputes.[38] Vero argues that in this case, the valuers retained by the parties had expressed widely differing views about the value of the insured building, with Vero's valuer assessing a market value for the buildings of $370,000 but a depreciated replacement cost of $1,400,000. Prattley's valuer assessed the market value as $1,050,000 after considering various approaches to valuing the building, including depreciated replacement cost, which he assessed at $1,021,000.

[225] On the basis of facts known to Vero, it was entirely open to Vero to consider that market value was likely to be the appropriate measure of indemnity in this case and it could have argued on the basis of a valuation that the building's market value was well below the figure assessed by Prattley's valuer. Equally, it is clear that Prattley left no stone unturned in endeavouring to maximise the valuation and I am

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36 There were, during the negotiations, threats by Prattley to bring in lawyers making it clear litigation was an option.

37 *Couch v Branch Investments (1969) Ltd* [1980] 2 NZLR 314 (CA) at 335.

38 Citing *Miles v New Zealand Alford Estate Co* (1886) 32 Ch D 266 (CA); *Bank of Credit and Commerce International SA v Ali,* above n 32; *Moyes & Groves Ltd v Radiation New Zealand Ltd* [1982] 1 NZLR 368 (CA) at 371.

satisfied that giving up the right to forego any other arguments which would increase its entitlement under the policy, was valuable consideration.

[226] In short, I accept, both because the obligation under the policy was to pay an unliquidated amount and also because both parties gave up valuable rights and entered into the agreement in good faith, this is a valid and binding agreement of compromise.

Conclusion

[227] I am satisfied that the Agreement is valid and binding. Notwithstanding that Prattley now considers it should have achieved a better outcome had its claim been assessed on an event by event basis and using depreciated replacement cost as the measure of loss, Prattley entered a contract settling its claim and there are powerful public policy reasons for that agreement being enforced and upheld.

[228] While I accept that "the Court will be very slow to infer that a party intended to surrender rights and claims of which he was unaware and could not have been aware", in the present circumstances the clear language of the Agreement precludes Prattley from revisiting its entitlement under the policy simply because it now has a revised view about how its entitlement might be calculated that it did not have when it entered the Agreement.[39] This is because the wording of the release in cl 4 made it:[40]

> … plain that the parties intended that the release should not be confined to known claims … part of the object was that the release should extend to any claims which might later come to light. The parties wanted to achieve finality. … The risk that further claims might later emerge was a risk the person giving the release took upon himself. It was against this very risk that the release was intended to protect the person in whose favour the release was made.

[229] It is not a case where the further claim could be said to be outside the contemplation of the parties at the time it was entered into, because it was related to a subject matter which was not under consideration when the agreement was made.[41]

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39 *Bank of Credit and Commerce International SA Ltd v Ali,* above n 32 at [10].
40 Per Lord Nicholls at [27].
41 As was discussed in *Bank of Credit and Commerce International SA Ltd v Ali,* above n 32.

The calculation and quantification of Prattley's entitlement under the policy, which is what Prattley seeks to reopen, is precisely what the Agreement was intended to resolve.

[230] This can also be illustrated by exploring the counter proposition, which is whether it would be acceptable to Prattley if Vero sought to reopen the Agreement because the valuation provided by Prattley was not, as it said on its face, based on net rentals, but on artificially inflated gross rentals for the building. Undoubtedly Prattley would have resisted reopening the claim, because it saw the security of retaining the $1,200,000 payment as a valuable outcome which it did not expect to have threatened by subsequent litigation.

[231] For all these reasons, I am satisfied that the Agreement should be upheld and, even if Prattley's entitlement was negotiated on an incorrect understanding of how the policy obligations should be met in Prattley's circumstances, Prattley cannot revisit the agreed settlement.

Vero's counterclaim

[232] Clause 2 of the Agreement provides that Prattley will:

> … indemnify and hold harmless Vero against all claims (including all defence costs) that may be made against Vero by any person or entity alleging that they have … any right to any benefit under the policy in relation to the Property Damage.

[233] Vero argues that the present claim by Prattley comes within this clause, as it is a claim alleging that Prattley itself has a right to benefit under the policy in relation to the damage to the building. Vero argues that this clause was an important aspect of the benefit that Vero purchased by agreeing to pay the settlement sum by ensuring that the insurer would not be exposed to further costs in connection with the claim including from a third party. It says that there should be no difference to the application of the clause whether it is Prattley itself, or a third party, which endeavours to reopen the claim. The same policy considerations that support giving effect to settlement agreements support the enforcement of the indemnity provisions.

[234] Prattley, however, argues that cl 2 is directed to a different issue, which is where a person other than the settling party asserts an interest in the insured property. In that case it accepts Vero is entitled to claim indemnity costs under the High Court Rules.

[235] The answer, of course, turns on the proper construction of this provision, so that the Court gives effect to what the contracting parties intended (as objectively assessed). That requires me to read the terms of the contract as a whole, giving the words their natural and ordinary meaning in the context of the Agreement, the parties' relationship, and all the relevant facts surrounding the transaction so far as they were known to the parties.

[236] In that regard, I look to the language of the preceding clause which states:

> The Insureds warrant that:
>
> a. They have no other insurance that may cover the Property Damage; and
>
> b. No other person or entity has an interest in the Insured Property.

[237] The juxtaposition of that clause before cl 2 is significant. Clause 1 separately identifies "the Insureds" (being Prattley) and any other "person or entity" that might have an interest in the insured property. The same distinction is made in cl 2, so the only natural way of reading cl 2 is that the reference to any "person or entity" is a reference to a party other than the entity which is defined as "the Insureds".

[238] Furthermore, in the context of the Agreement where it is not contemplated that Prattley will raise any other claim for the reasons discussed above, it could not have reasonably been in the contemplation of the parties that cl 2 would extend to Prattley.

Costs

[239] I accept that Vero has signalled it is seeking indemnity costs, or at least increased costs, in all the circumstances. It also signals that it wants the Court to reserve leave to Vero to apply for costs directly against Risk Worldwide in the event that costs awarded against Prattley are not paid. It is clear that the issue of costs may

be complex and it was not fully addressed by the parties at the hearing. It is an appropriate case in which to reserve costs.

[240] If costs are not resolved by agreement, memoranda are to be exchanged as follows:

(a) Vero's costs submissions, not exceeding 10 pages, to be filed and served within 20 working days of this decision;

(b) Prattley's costs submissions, again not exceeding 10 pages, to be filed and served within 30 working days from the date of this decision; and

(c) any submissions in reply by Vero, limited to five pages, to be filed and served within 35 working days following the date of the decision.

[241] In the event this decision is appealed, the above timetable may be deferred on the request of either party, until all appeals are resolved.

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