IN THE COURT OF APPEAL OF NEW ZEALAND

CA563/2013
[2014] NZCA 76

BETWEEN	SKYWARD AVIATION 2008 LIMITED Appellant
AND	TOWER INSURANCE LIMITED Respondent

CA709/2013

BETWEEN	TOWER INSURANCE LIMITED Appellant
AND	SKYWARD AVIATION 2008 LIMITED Respondent

Hearing:	27 November 2013
Court:	Randerson, Harrison and Miller JJ
Counsel:	N R Campbell QC and KP Sullivan for Appellant R B Stewart QC and M C Smith for Respondent
Judgment:	20 March 2014 at 3 pm

JUDGMENT OF THE COURT

A The appeal against the High Court judgment answering questions 1 and 2 is allowed.

B The appeal against the judgment answering question 3 is dismissed.

C The respondent's appeal against the decision not to award costs in the High Court is dismissed.

D The respondent is ordered to pay 80 per cent of the appellant's costs for a standard appeal on a Band A basis together with usual disbursements. We certify for two counsel.

REASONS OF THE COURT

(Given by Harrison J)

Introduction

[1] The aftermath of the Christchurch earthquakes in September 2010 and February 2011 has generated extensive litigation between property owners and their insurers. This appeal arises as a consequence of earthquake damage both to a house and the land on which it is situated. The property is within what is known as the red zone, an area of land designated by the Christchurch Earthquake Recovery Authority (CERA) where repair would be prolonged and uneconomic. The owner of the property, Skyward Aviation 2008 Ltd, has accepted CERA's offer to buy the land at its then current rating value and pursued claims for loss of the house against the Earthquake Commission (EQC) and Skyward's insurer, Tower Insurance Ltd (Tower).

[2] Skyward has since settled its claim against EQC. But it could not agree with Tower on the basis for or measure of its insured loss under a full replacement value policy. Skyward asserted that it was entitled to payment of an amount equal to the estimated costs of rebuilding or repairing its house on the land and issued a proceeding against Tower claiming damages. Tower countered that it had the right to choose from a variety of settlement options under the policy and that it was obliged to pay only the fair price of a replacement house elsewhere of comparable size, construction and condition as Skyward's house was when it was new.

[3] Skyward's property in Burwood comprised 1,533 square meters. On it were an early 20th century villa and a separate sleep out. Both were rented to residential tenants. Skyward has settled its claim against Tower for loss of the sleep out which does not require further consideration.

[4] Skyward bought the property in 2009 for $450,000.00 and insured the house with Tower. The certificate of insurance did not nominate a sum insured, providing instead that the house was insured for its full replacement value based on 210 square

meters being built in 1900 with a $1,000.00 excess and EQ cover of $112,500.00. The house was damaged by earthquakes on 4 September 2010 and 22 February 2011 caused by liquefaction, burst sewage pipes and ground displacement. The land was also damaged.

[5] In 2007 the property had a rating value of $582,000.00, divided equally between $291,000.00 for the land and $291,000.00 for improvements. Skyward gave Tower notice of its intention to accept CERA's offer of $291,000.00 for the land. Tower did not object. Its statement of defence to Skyward's statement of claim pleads that the house was economic to repair. Nevertheless, because the property was in the red zone, Tower was willing to make a cash offer based on the cost of repair.

[6] Skyward has received a total of approximately $659,000.00, being: (1) $291,000.00 from CERA for the land; (2) $203,000.00 from the EQC for house damage (being the limit of the EQC's statutory liability);[1] and (3) approximately $165,000.00 from Tower for house damage based on the cost of purchasing a comparable house elsewhere. Tower's payment was made without prejudice to Skyward's right to claim more. Tower says Skyward is not entitled to anything more for the house than it has received from EQC and Tower together. It says that the pre earthquake market value of the property was $492,000.00, divided between land at $275,000.00 and house and chattels at $217,000.00; and that Skyward could buy a similar house – excluding the land – for $365,000.00. Skyward says the house could be repaired on the site at a cost of $682,525.00 or rebuilt elsewhere to regulatory standards for $770,960.00.

[7] These figures reflect the financial difference in the parties approaches; they are at least $300,000.00 apart. The difference would be compounded if another $150,000.00 were factored in for the cost of constructing special foundations for a house in the red zone. But Mr Campbell QC accepts, following the judgment of Asher J in *O'Loughlin v Tower*,[2] that Skyward is not entitled to claim that cost in circumstances where it will not in fact rebuild in the red zone.

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1 Earthquake Commission Act 1993, s 18, .

2 *O'Loughlin v Tower Insurance Ltd* [2013] NZHC 670, [2013] 3 NZLR 275 at [162]–[163].

[8] In summary, Tower says that (a) it has a contractual right to elect to settle Skyward's claim by paying the company an amount equal to the cost of buying a comparable house elsewhere because that would be the most economic option available; (b) its payments made to date are sufficient to discharge that obligation; and (c) settlement according to Skyward's measure would be contrary to settled principles of indemnity because the company would recover some $975,000.00 for a property which it bought in September 2009 for $450,000.00 and which had a pre earthquake market value of $492,000.00.

[9] In an attempt to resolve their differences the parties agreed to submit these three questions to the High Court for determination:

> (1) under the terms of the insurance policy, on what basis is the amount payable by Tower to be calculated if an insured party's claim is to be settled by Tower paying the cost of buying another house;
>
> (2) under the terms of the policy, is it Tower's choice whether the claim is to be settled by paying the cost of buying another house or, if Tower settles by making payment, whether it is to be made based on the cost of rebuilding, replacing or repairing the house; and
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> (3) did Tower make an irrevocable election to settle Skyward's claim by making payment based on the full replacement value.

[10] David Gendall J answered all three questions in Tower's favour.[3] Skyward now appeals. The general issues are, first, which party decides whether and where to repair or rebuild the house or purchase another house and, second, once that decision is made, what Tower is bound to do or pay to meet its obligation to the insured party.

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[3] *Skyward Aviation 2008 Ltd v Tower Insurance Ltd* [2013] NZHC 1856.

Insurance Policy

[11] The parties entered into what is described as a "Provider House (Maxi Protection) Policy", insuring Skyward against "[s]udden and unforeseen accidental physical loss or damage" to property. The policy contemplates various kinds of loss; not only natural disaster but also, for example, fire.

[12] In the event of damage to the house caused by a natural disaster, Tower's financial obligation is limited to payment of "the difference between the amount paid under the EQ cover and the sum insured shown in the certificate of insurance".[4] In other words, the policy provides what is known as topup cover for natural disaster damage, as is customary for domestic policies. EQC cover is capped at $100,000 per event.

[13] The parties' differences start with this insuring provision:

> **HOW WE WILL SETTLE YOUR CLAIM**
>
> **We** will arrange for the repair, replacement or payment for the loss, once **your** claim has been accepted.
>
> **We will pay**:
>
> the **full replacement value** of **your house** at the **situation**; or
>
> the **full replacement value** of **your house** on another site **you** choose. This cost must not be greater than rebuilding **your house** at the **situation**; or
>
> the cost of buying another house, including necessary legal and associated fees. This cost must not be greater than rebuilding **your house** on its present site; or
>
> the **present day value**;
>
> as shown in the **certificate of insurance**.
>
> **We** will only allow **you** to rebuild on another site or buy a house if **your house** is damaged beyond economic repair.

[14] The policy has these definitions of terms "full replacement value" and "present day value":

> ***Full replacement value*** means the costs actually incurred to rebuild, replace or repair **your house** to the same condition and extent as when new and up to the same area as shown in the **certificate of insurance**, plus any decks, undeveloped

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[4] Emphasis omitted. The certificate of insurance was issued by Tower to Skyward when the company first insured the property and materially provided that the house was insured for "FULL REPLACEMENT based on Area Sq Metres 210."

basements, carports and detached domestic outbuildings, with no limit to the sum insured.

Present day value means the cost at the time of the loss or damage of rebuilding, replacing or repairing **your house** to a condition no better than new and up to the same area as shown in the **certificate of insurance**, plus any decks, undeveloped basements, carports and detached domestic outbuildings, less an appropriate allowance for depreciation and deferred maintenance, but limited to the market value of the property less the value of the land as an unoccupied site.

[15] The "basis of settlement provisions" are qualified as follows:

In all cases:

…

we have the option whether to make payment, rebuild, replace or repair **your house**;

…

we will use building materials and construction methods commonly used at the time of loss or damage.

[16] The policy limits Tower's financial obligations in this way:

We are not bound to:

…

pay more than the **present day value** if **you** have **full replacement value** until the cost of replacement or repair is actually incurred. If **you** choose not to rebuild or repair **your house** or buy another house **we** will only pay the **present day value** and the reasonable costs of demolition and removal of debris including contents;

pay the cost of replacement or repair beyond what is reasonable, practical or comparable with the original;

repair or reinstate **your house** exactly to its previous condition.

Decision

[17] The parties' identification of three discrete questions of law spares us from determining any factual disputes. On appeal, counsel addressed argument by reference to all three questions. We agree with Mr Stewart QC that the second question should be addressed first: it is logical to decide the correct basis for settlement before addressing the appropriate measure.

(1) What is the basis of Tower's liability?

(a) Principles

[18] The relevant principles are well settled.[5] This policy is a contract of indemnity whereby the insurer agreed to compensate the insured for sudden and unforeseen physical loss or damage to its house. Cover was extended to full replacement value to compensate the policyholder for depreciation by providing for repair or replacement on a "new for old" basis. This express agreement places in perspective Tower's complaint that Skyward is claiming substantially more than the property's market value at the time of the earthquakes: Skyward is indeed doing that, but only because Tower agreed to provide full replacement cover.

(b) Basis of settlement

[19] The policy provides four alternative bases for settlement:

(1) The full replacement value of Skyward's house at its situation. That means the costs actually incurred to an unlimited amount in rebuilding, replacing or repairing the house to the same condition and extent as and when new and up to the same area as shown in the certificate of insurance;

(2) The full replacement value of the house at another site chosen by Skyward, providing the cost is no more than the cost of rebuilding the house on its existing site. However, to make sense, the provision must extend to replacement or repair as referred to in the full replacement value definition and also to notional, not actual, costs. Otherwise there is no available comparative measure for fixing the costs of building on another site;

(3) The cost of buying another house. This alternative is subject only to the same limitation as the first two alternatives – the cost must not be

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[5] *CIC Insurance Ltd v Bankstown Football Club Ltd* (1997) 187 CLR 384 at 395–400.

greater than the cost of rebuilding the house on its existing site. While this alternative does not use the phrase "full replacement value", that is the effective limit introduced by the words "this cost must not be greater than the cost of rebuilding … on [the] present site." The policy uses the words "on its present site" for this alternative whereas the first two alternatives use the words "at the situation". However, as the definition of "situation" confirms, the three alternatives are referring to the present or existing site. Also, as with the second alternative, the calculation is of notional, not of actual, rebuilding costs.

(4) The present day value, which is defined as the cost of repair or replacement less depreciation, but limited always to the market value of the house when damaged less land value. No question arises of Skyward settling for present day value, but as will be seen there are circumstances in which that is the correct measure of payment.

[20] Two matters are not in dispute. One is that Tower is not bound to pay anything more than present day value until Skyward incurs the cost of reinstatement, rebuilding or replacement. The other is that, as David Gendall J correctly found, Tower had reserved the right to indemnify either by making payment or by rebuilding, replacing or repairing the damaged house;[6] that is, to choose between payment or reinstatement. The Judge effectively read into the relevant basis of settlement provision a disjunctive "or" to this effect:

> In all cases we have the option whether to make payment [or] rebuild, replace or repair your house.

(c) Who has the right to decide?

[21] The real inquiry is into which party has the right after a claim is made to decide whether the house will be repaired, rebuilt or replaced, before considering the appropriate basis of payment. David Gendall J initially appeared to accept that Skyward, not Tower, was entitled to determine what happened; he gave detailed practical examples of how the company, not the insurer, would implement the choice

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6 At [36], following *O'Loughlin*, above n 2, at [162]–[163].

between the four alternatives.[7] But the Judge later reached a contrary view. He relied on the words "in all cases" in the basis of settlement provisions as giving Tower "the option whether to make payment, rebuild, replace or repair", following Asher J's conclusion in *O'Loughlin* that:

> [168] Tower has the choice, therefore, of whether to make a payment, or rebuild, replace or repair. It follows that Tower, in making the payment, can choose the basis of payment. That basis must be on a repair, rebuild or replacement basis, and if repair is not an option, which I have found it is not, Tower can choose between rebuild and replacement.

[22] However, these contractual provisions point strongly toward the decision being that of the policyholder:

(1) Tower reserves the right to pay only present day value "if you [the insured] choose not to build or repair your house, (the first alternative) or buy another house (the third alternative)"

(2) Tower reserves the right to disallow Skyward from either building on another site (the second alternative) or buying a house (the third alternative), if the existing house is not damaged beyond economic repair. This right of veto could only be exercised once Skyward had made the underlying choice. In other words, it assumes that Skyward is generally at liberty to make the choice, then restricts the company's ability to choose options two or three to the case where the existing house is not economically repairable;

(3) The second alternative provides for full replacement value of the house "on another site you [the insured] choose" – that is, it is the insured's right to choose;

[23] These provisions are consistent with the parties' respective interests in the property. The insured owns it, with all that ownership entails, while the insurer has undertaken to settle a claim by indemnifying the insured for loss or damage up to a certain measure and so has a strictly economic interest. Three observations follow.

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[7] At [42(b)].

First, only to the extent that the policy restricts its options should the policyholder be deprived of its control over repair, rebuilding or sale of its property. Second, once it is established that the insurer must pay the full measure of loss, it should be indifferent to the policyholder's decision about how to reinstate the property. Third, until that point the insurer has a direct interest in how the claim is settled, since that decision will determine how much it will pay.

[24] In our judgment these provisions must prevail over the statement in the basis of settlement provision that in all cases Tower has the option to make payment, rebuild, replace or repair the house. While accepting that the policy allows Tower to insist on repair in certain situations, we do not accept that it allows Tower to control what happens in every case. If it did, as Mr Campbell observed, Tower might choose to pay on a present value basis, that being one of the settlement options, notwithstanding that the policyholder wished to reinstate or replace the house.

[25] We observe too that words must be read into the basis of settlement provision to make it sensible. Notably, the words "make payment" must mean "payment to the policyholder", as Mr Stewart appeared to accept. Every basis of settlement involves Tower making a payment, though in some cases it may be made to a contractor whom Tower has engaged to make repairs.

(d) Alternative bases

[26] We now examine the various bases of settlement in light of our conclusion that the policyholder ultimately has the right to decide what to do with the insured property. To begin with, it is obvious that if the policyholder does not pursue full replacement by repair, rebuilding or replacing, Tower is bound only to pay the present day value as defined. If the policyholder wishes to repair, rebuild or replace to full replacement value, Tower's rights depend on whether the house is economically repairable. If it is, Tower may insist on repair or rebuilding on the same site. Further, Tower may commission the work. The reasons are obvious; the costs of repair or rebuilding are at the insurer's risk so it will wish to control the costs, and to decide whether repair or rebuilding is the better option.

[27] If the house is not economically repairable, then the policyholder may decide whether to repair or rebuild on the existing site, or rebuild elsewhere, or buy another house. But in every such case Tower need only pay the cost of rebuilding on site. Again, the reasons are obvious; the insurer is in this case committed to pay the full measure of replacement cost, and is indifferent to how the insured spends it.

[28] Mr Stewart resisted this analysis, and advanced a number of arguments in support of the Judge's eventual conclusion. First, he submitted that the natural construction of a clause which provides for alternative methods of performance is that the promisor has the choice between the methods of performance.[8] However, this statement of principle does not assist where the terms of the contract provide otherwise.

[29] Second, Mr Stewart submitted, Tower's express right to choose between making payment or rebuilding, replacing or repairing bears an implicit right to choose between the bases of payment; and it would be inconsistent for Tower to be given the choice whether to reinstate itself or pay but for the insured to be given the choice between alternative bases of payment. However, we see no inconsistency in allowing the insured party to choose where the measure is effectively the same. Once it is established as a matter of fact that the house is not economically repairable, Tower has no continuing interest in whether the insured party rebuilds on the existing site, rebuilds on another site or buys a house elsewhere, subject only to the insured actually incurring replacement cost, and further to the agreed financial limits.

[30] Third, Mr Stewart argued, Tower's choice of the basis of payment is also confirmed by the limitation on Skyward rebuilding on another site or buying a house only if the existing house is damaged beyond economic repair. No purpose would be served by this clause, he says, if the choice between the bases of payment was for the insured. Its purpose is to give Skyward fair notice of how Tower intends to exercise its choice, and the concept of Tower allowing the insured to rebuild on another site or buy a house implicitly recognises Tower's choice whether this will be done.

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[8] H G Beale, *Chitty on Contracts* (31st ed, Sweet & Maxwell, London, 2012) at [21-006].

[31] This construction of the proviso contradicts its plain language, and we reject it. Its purpose is to impose a limitation on the nature and scope of the insured's underlying right to choose between alternatives, allowing the insurer to restrict the extent of its liability. It cannot be construed as a notice provision.

[32] Fourth, Mr Stewart recognised the legitimacy of an insured party's underlying interest in being able to rebuild on an alternative site or buying another house in a location where it retains neighbourhood links. However, he says that interest must be balanced against Tower's interest as insurer in having the choice between the most economic means of replacing the insured property. In this case, he says, the parties have agreed that Tower's interest should prevail. In any event, he says, the insurer would act reasonably and attempt to agree on an amicable settlement with the insured party; it would choose the third alternative – buying a house elsewhere – as a last resort, to be available if a reasonable settlement was not possible.

[33] We reject this submission. Mr Stewart's argument appears to presuppose that in exercising its right to choose between any of the three alternatives Tower is not bound by the limitations applying to Skyward; that is, Tower's right to choose between the three is absolute, regardless of whether the house is damaged beyond economic repair. As we have emphasised, this policy provides for indemnity either by payment or reinstatement. It would be surprising if the insurer's primary election of whether to pay or reinstate determined whether the insured was able to rebuild on the existing site, on another site or had to buy a house elsewhere.

[34] Taken to its logical conclusion, Tower's argument would allow it to force the insured party to relocate to another city. The words should not be construed to reach that extreme result and deny an insured party's legitimate interest unless the words point unequivocally to that result. The insured party's legitimate interest in remaining in an area is best recognised by the means adopted by the parties of allowing it to choose where to spend the reinstatement moneys.

[35] We add that Mr Stewart's assurance that Tower would act reasonably and only exercise the third alternative of buying another house as a last resort undermines his argument. David Gendall J gave this point weight as follows:

> [74] At a practical level, Mr Stewart QC indicated that in situations such as the present, Tower will endeavour to reach agreement with its policyholders amicably on the method of settlement of their claims and is usually able to do so. Payments made on the basis of the estimated cost of reinstatement, or for the purchase of a comparable replacement property, can be agreed. However, where agreement cannot be reached and there is a significant monetary gap between the parties, as seems to be the case here, ultimately Tower can choose which of the settlement options under the policy it will adopt in relation to the insured's claim. If Tower chooses to indemnify the insured for the cost of buying another comparable replacement house, this cannot be said, however, to "force" the customer to buy that house. It simply means that, if Skyward chooses not to accept payment on this basis to settle its claim, Tower's payment will be limited to the pre-earthquake market value of the house, until such time as actual costs of rebuilding or replacing the house are incurred by Skyward.
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> [75] In this scenario, Skyward, as the insured, would not be out of pocket because it has not incurred the cost of actually replacing the Kingsford Street house and would still receive the cash value of its asset before the loss. Therefore, it could be said that Skyward is indemnified for its actual loss.

[36] With respect, we disagree with the Judge. An assurance that an insurer will act reasonably, but subject always to its overriding legal rights to act otherwise, is of little assistance in construing the terms of a policy. Moreover, Tower would be effectively forcing Skyward to settle on present day value rather than the agreed measure of full replacement value if the company did not accept the insurer's offer to buy a comparable house on another site. And the example given by the Judge suggests that Tower is entitled to dictate a present day value settlement unless Skyward repairs or replaces the existing house in circumstances where it is not possible to rebuild on the existing site or elsewhere.

[37] We accept Mr Stewart's observation that an insurer will always wish to avail itself of the most economic way of discharging its contractual obligation to an insured party in the event of loss or damage to property. However, Tower drafted this policy and we can only assume it was satisfied that it had secured that objective by reserving to itself (a) the right to make the underlying choice between payment or reinstatement and (b) a condition that the house must be uneconomic to repair before Skyward is entitled to exercise a right of election. An insurer cannot rely on a

general statement of economic desirability to override the express or clearly implied provisions of its policy. The position may be otherwise if the contract had stated expressly that it was the insurer's right to choose between the alternative bases for payment. But this policy did not so provide.

[38] It follows that we are respectfully satisfied that David Gendall J and Asher J in *O'Loughlin* erred on this point. However, we would add that we have had the benefit of argument from Mr Campbell. He did not appear in the High Court in this litigation or in *O'Loughlin* and his submissions in this Court suggest that Skyward's case was more focused before us than it was before David Gendall J. Both Judges may well have reached a different conclusion if they had enjoyed the same benefit.

[39] Accordingly, the answer to the first question is that, once it has been established that the house is not economically repairable, Tower has no right to choose the basis of settlement. It is then for the insured, not Tower, to decide whether to rebuild (or repair) on site, or to rebuild elsewhere, or to buy another house. Of course it must incur these costs before Tower need pay anything more than the appropriate measure of present day value.

(2) What is the correct measure of Tower's liability?

[40] David Gendall J was asked to determine the correct measure of Tower's liability where it settles by paying the cost of buying another house. He decided that Tower's obligation is subject to this further limitation:

> [58] In terms of this first question outlined at [44] above, the amount to be payable by Tower, where it is to pay to Skyward the cost of buying another house, is to be the fair price of a replacement house which is to be a reasonable and practical extent comparable, of the same 207 m² [sic] size and construction (as far as may be possible), in the same condition, and of the same style and extent (more or less), as the Kingsford Street house was when new. This could be a new or (more likely) a second hand house sited outside the red zone. As to whether its size, construction and quality were reasonably comparable, these would all be determined on the facts of this particular case. In this regard, the broad house features in the example I have provided at [53] above might, to some extent assist. For valuation purposes, as I see it, such a reasonably comparable replacement house might first be identified and then be the subject of one agreed valuation (or alternative independent valuations) to arrive at that fair replacement price. And finally, of course, payment by Tower would be subject to the provisos noted at [46](c) and [49] above.

[41] The rationale for the Judge's conclusion is found earlier in this passage:

> [46] How then is the amount of the payment which Tower must make to be calculated in terms of the policy if Skyward's claim here is to be settled by Tower paying the cost of buying another house? The answer to this question, as I have noted above, is simply that Tower's obligation under this replacement option is the same in principle as that for a repair or rebuild and requires:
>
> (a) As a fundamental starting point, a proper consideration of the size, construction, condition, style and extent of the house as when new on a sound site; and
>
> (b) An obligation on Tower to indemnify Skyward for actual costs incurred to replace the house to this condition, to the extent replacement in such a manner is reasonable, practical and comparable with the original; and
>
> (c) The obligation on Tower is subject to the proviso that it is not obliged to pay more than the notional cost of rebuilding the house on its existing Kingsford Street site.

[42] With respect, we disagree that the policy provides the limitation which David Gendall J held was imposed on Tower's obligation. The maximum amount payable by Tower as prescribed by all three relevant alternatives is materially the same. The first two alternatives expressly adopt full replacement value - that is, the cost of rebuilding, replacing or repairing the house to the same condition and extent as new – at its present site. The third alternative adopts the notional costs of rebuilding on the existing site, the same limitation applying to the second alternative and one of the three reinstatement measures used in the definition of "Full Replacement Value". The amount payable by Tower if Skyward buys another house is not subject to any other limitation. In essence, the policyholder is not obliged to choose a house of comparable size, construction, condition and style as its existing house once it is agreed that its existing house is damaged beyond economic repair.

[43] Mr Stewart advanced a number of arguments to the contrary. First, he relied upon the express limitation on the insurer's obligation to pay no more than "the cost of replacement or repair beyond what is reasonable, practical or comparable with the original." He accepted that the words "comparable with the original" mean "comparable with the original as when new". He says that the limitation extends to Tower's obligation to pay for the cost of buying another house.

[44] We do not accept this submission. The contractual limitation does not extend to buying another house or in any way affect the measure agreed between the parties. The measure of loss adopted by the third alternative is straightforward. As Mr Campbell submitted, Tower must pay the cost of buying another house including fees once the house is bought. We agree that the only limitation is that the cost must not be greater than the cost of "rebuilding your house on its present site". There is no other control or limit on the size, style or quality of the other house. It is implicit in this provision that if Skyward buys a house at a greater cost, Tower's contribution will be capped at the agreed level with Skyward meeting the difference from its own resources.

[45] Second, Mr Stewart submitted, adoption of Skyward's position would not return to it what it has lost but give it something different and better, a result which is contrary to the principle of indemnity. He refers to the valuation evidence to the effect that the cost of rebuilding the house on good ground would be between $712,000.00 and $770,960.00. Skyward would therefore receive between $860,000.00 and $920,000.00 as the measure of its loss when a comparable house would cost about $365,000.00 and its pre-earthquake market value was $211,000.00. He says that acceptance of Skyward's argument would give the company more than the full indemnity.[9]

[46] We do not accept this submission. We are not materially assisted in answering a discrete question of contractual interpretation by the insurer resorting to an assessment of what the insured will receive if its argument is upheld. The parties have agreed that the insurer's financial obligation will be measured in one of two alternative ways. One is the traditional measure of indemnity reflected in an obligation to pay present day value for damaged property – that is old for old – if the insured party takes no steps to repair the house, rebuild on another site or buy another house elsewhere. The other is full replacement value or new for old where the insured party decides to reinstate. The parties' agreement to this effect does not and cannot offend any principle of indemnity.

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[9] Indemnity being a fundamental principle of insurance law: *Castellain v Preston* (1883) 11 QBD 380 (CA) at 386, per Brett LJ.

[47] Third, Mr Stewart submitted, the other settlement options under the policy do not depart from the principle of indemnity. He refers to the default settlement option where if no reinstatement work is done the measure of loss is present day value – the market value of the property at the date of loss. That is all an insured party has lost if it does not take any steps to replace. Here, however, if Skyward is paid the currently estimated rebuilding cost when it does not intend to rebuild, it would be receiving more than 300 per cent above the market value of the house at the date of loss.

[48] This submission is a variation on its predecessor and does not assist Tower. It is now common ground that Skyward is not entitled to payment of an amount equivalent to the currently estimated rebuilding cost on the existing site unless and until it either rebuilds on another site or buys a house elsewhere. The parties have agreed that if Skyward does not take either of these steps it will only be entitled to indemnity in an amount equal to present value. The constant and absolute answer to Tower's various arguments on indemnity is that the parties have agreed on two alternative bases for indemnity where Skyward's choice of one, subject to the agreed conditions, will necessarily mean that Tower's liability is greater than it would be if the other measure was chosen.

[49] Accordingly, we are satisfied that the Judge erred in answering this question. We are satisfied that if Skyward buys another house Tower is bound to pay the cost of that house up to the cost which Skyward would notionally incur in repairing its existing house to the same condition and extent as and when new and up to the same area as shown in the certificate of insurance.

(3) Did Tower irrevocably elect to make a payment based on full replacement value?

[50] We can deal with this question briefly.

[51] Skyward pleaded that by emails sent on 9 September 2011, 29 November 2011 and 8 March 2012 Tower made an irrevocable election to settle Skyward's claim by making payment based on a full replacement value. Determination of this

question is essentially one of fact. Gendall J undertook an exhaustive analysis of the relevant evidence.[10] He was satisfied that the emails did not constitute an irrevocable election by Tower to settle the claim by paying full replacement value without more.[11]

[52] Skyward appealed against this finding. However, Mr Campbell addressed only brief argument in support. He did not attempt to challenge the basis of the Judge's findings. We are not satisfied that Tower made an irrevocable election of the type pleaded nor are we satisfied that the Judge erred in answering this question in Tower's favour. In any event, the question is now moot given our answers to the first two questions.

Result

[53] Skyward's appeal against the High Court judgment answering questions 1 and 2 is allowed. Its appeal against the judgment answering question 3 is dismissed.

[54] In the High Court David Gendall J declined to make an award of costs in Tower's favour. He was satisfied that costs should lie where they fall. Tower appeals. The arguments advanced by Tower in challenge to that decision proceeded on the premise that it would succeed in this Court. The result of Skyward's success would normally mean that it would be entitled to costs in the High Court. However, the same principles on which it successfully relied in the High Court still prevail. An additional factor is that considerable argument was devoted in the High Court to Skyward's identification and pursuit of question 3. The costs appeal is dismissed.

[55] Skyward has been successful on its two principal grounds of appeal in this Court. Costs must follow the event but an allowance is necessary for the fact that its appeal on the third question was unsuccessful. Tower is to pay 80 per cent of Skyward's costs for a standard appeal on a Band A basis together with usual disbursements. We certify for two counsel.

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[10] At [77]–[120].
[11] At [120]

Solicitors:
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Gilbert Walker, Auckland for Respondent