**IN THE COURT OF APPEAL OF NEW ZEALAND**

**CA281/2014**
**[2015] NZCA 13**

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| BETWEEN | HELEN KRAAL AND BRUCE ROBERTSON IRVINE<br>Appellants |
| AND | EARTHQUAKE COMMISSION<br>First Respondent |
| | ALLIANZ NEW ZEALAND LIMITED<br>Second Respondent |

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| Hearing: | 13-14 November 2014 |
| Court: | Wild, Simon France and Asher JJ |
| Counsel: | N Campbell QC, C R Johnstone and R Hargreaves for Appellants<br>J A Knight, A Neris and N J Bruce-Smith for First Respondent<br>I J Thain and K R Pengelly for Second Respondent |
| Judgment: | 13 February 2015 at 3 pm |

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**JUDGMENT OF THE COURT**

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**A The appeal is dismissed.**

**B The appellants must pay the respondents' costs for a standard appeal on a band B basis and usual disbursements. We certify for second counsel for each respondent.**

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**REASONS OF THE COURT**

(Given by Asher J)

## Introduction

[1] This appeal arises out of the catastrophic earthquakes in Christchurch. It concerns the claim of the appellants, Helen Kraal and Bruce Robertson Irvine, that they are entitled to insurance cover of their house under the Earthquake Commission Act 1993 (the ECA). Their claim results from the Christchurch City Council (the Council) prohibiting any occupation of their property due to a significant and ongoing risk from rock fall.

[2] The first respondent, the Earthquake Commission (EQC), is the successor of the Earthquake and War Damage Commission.[1] The second respondent, Allianz New Zealand Ltd (Allianz), is an insurer that insured the home of Ms Kraal and Mr Irvine under a Premier (Accidental Damage) Replacement House Policy.

[3] In the High Court, Mallon J held that the Council was not liable to pay the replacement value of the appellants' house because their property had not suffered "natural disaster damage".[2] In particular, she held that the definition of natural disaster damage, "physical loss or damage to the property", required physical disturbance to the property, and did not extend to claims for losses (such as loss of the right to occupy) which did not arise from physical disturbance. The primary issue on appeal is whether this is a correct interpretation of "natural disaster damage" in the context of the ECA.

## Background

[4] The property in question is at 119 Wakefield Avenue, Sumner (the property). At the time of the earthquakes, Ms Kraal and her partner lived there. They had lived there for 18 years and had raised two children there. The property had been purchased by her and Mr Irvine as trustees of the Helen Kraal Family Trust. We will refer to the appellants and occupiers collectively as Ms Kraal, as she is both a joint trustee and an occupant.

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1 Earthquake Commission Act 1993, s 4.

2 *Kraal v Earthquake Commission* [2014] NZHC 919, [2014] 3 NZLR 42 [High Court judgment].

[5] The house is situated on the eastern side of the road. There is a flat area on the western side of the road opposite Ms Kraal's house that rises to an area of rocks and the steep face of Richmond Hill, which is part of the Port Hills.

[6] The two major Christchurch earthquakes occurred on 4 September 2010 and 22 February 2011. The house suffered some structural damage, including damage to the foundations. It is accepted that this damage is repairable and this proceeding is not concerned with that damage.

[7] The earthquake of 22 February 2011 caused widespread rock falls in the Port Hills. Thousands of rocks or boulders were dislodged and rolled down the hills. Almost 70 boulders landed in the vicinity of the property (from about 92 Wakefield Avenue to 107 Wakefield Avenue). No boulders landed on the property itself, but six boulders of reasonable size landed on the roadway and verge. Some rocks landed on the roofs of the properties on the western side of the road directly under the hills. In total five people in the Christchurch area died as a result of rock falls and cliff collapse. There was one death on Wakefield Avenue, near to Sumner Village some distance away.

[8] Ms Kraal lived at the property until the second earthquake. Shortly thereafter, on about 3 March 2011, Ms Kraal was required to leave the property under civil defence emergency powers.[3] Shipping containers were placed on the western side of Wakefield Avenue to protect motorists and pedestrians from boulders.

[9] The Council obtained a review of all Port Hills properties that had been subject to civil defence directions. Recommendations were made about the need for notices under s 124 of the Building Act 2004. Section 124(2)(d) empowers a territorial authority to issue a notice restricting entry to a building if it is satisfied that the building is a dangerous, affected, earthquake-prone, or insanitary building.

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[3] Civil Defence Emergency Management Act 2002, Part 5. See High Court judgment, above n 2, at [9].

[10] On 13 July 2011, the Council issued a s 124 notice in respect of the property stating that it was a dangerous building, and prohibiting persons from approaching or entering the building. There were further reports which assessed the property as being significantly at risk from rock fall.

[11] On 17 August 2012, the Canterbury Earthquake Recovery Authority (CERA) advised Ms Kraal that the property had been assessed as at risk from rock fall and was unlikely to reach what is known as an acceptable annual individual fatality risk in a timeframe extending beyond 2016. The s 124 notice expires on 18 April 2016.

[12] Ms Kraal has not lived in the house since the Council notices were issued. She has abandoned any hope of moving back into it and has since purchased another home with her partner. The house at 119 Wakefield Avenue remains damaged and unrepaired. Wakefield Avenue now features a line of abandoned houses and some vacant sections. Because the risk from rock fall is not anticipated to decline to pre-earthquake levels until 2021, there is potential for a further s 124 notice to be issued.[4]

[13] Ms Kraal has not challenged the s 124 notice. An engineering geologist that she engaged concluded that the property was dangerous due to the rock fall hazard.[5] It is not suggested that Ms Kraal has acted unreasonably in not challenging the s 124 notice. The shipping containers are not considered to be an effective long-term barrier for Ms Kraal's property.

[14] Mallon J in her decision concluded that the occupation of the property would not be permitted for the foreseeable future.[6] A seismic profile did not anticipate a reduction to pre-earthquake levels until 2021, by which time Ms Kraal would have been out of the house for 10 years. Even then the risk from rock fall might be at such an order of magnitude that it was possible that the Council would continue to regard the risk as unacceptable.

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4 At [22].
5 At [23].
6 At [30].

[15] On 24 September 2012, the Crown offered to purchase the property from Ms Kraal, and that offer was extended to 27 February 2015. The offer is based on the 2007 value of the property. The appellants have not made any decision on the offer and await the outcome of this appeal before making such a decision. The Crown offer has no bearing on the appellants' entitlements against the EQC and Allianz.

[16] EQC has declined to pay Ms Kraal for her losses resulting from not being able to occupy the house. Allianz has also declined to indemnify them under their insurance policy. Ms Kraal issued these proceedings seeking declarations that EQC was liable to pay the replacement value of their "residential buildings" up to the statutory limit, and that Allianz was liable to pay the difference between the EQC payments and the cost of rebuilding.

[17] The key issue that had to be determined in the High Court, and at issue in this appeal, is whether Ms Kraal's loss of the use of the house and its resulting unsaleability are "natural disaster damage" for the purposes of the ECA.

**The High Court judgment**

[18] Mallon J delivered a results judgment on 30 April 2014, and her reasons on 6 May 2014. We will refer to aspects of her judgment through this judgment. There is no challenge to the factual findings she made, including her conclusion that the appellants would be deprived of occupation of their home for the foreseeable future.

[19] In her reasons she held that a plain meaning of the relevant words in the ECA required physical loss to the property and not economic loss.[7] The context of the ECA, the relevant legislative history and case law supported such an interpretation.[8] She concluded:

> [68] In this case the loss suffered is loss of the ability to exercise a legal right that is part of the bundle of rights comprising the fee simple estate. It is not "physical loss … to the property". Loss in the context of the Act means loss to the physical materials or structure of the building. That interpretation is consistent with the natural and ordinary meaning of those words in the

[7] At [36]–[42].
[8] At [45]–[67].

> context of the Act. The legislative history does not suggest otherwise. To the extent that case law in the United States in respect of house insurance supports a different interpretation that case law is limited and should not be followed here. Case law in respect of other kinds of policies is of limited assistance but also does not support the interpretation advanced by the plaintiffs.

[20] She also determined that the Allianz policy required physical harm to the materials and structure of the building, and possibly imminent threats of such damage, and that Ms Kraal's loss was not "damage" under the policy.[9]

## Approach

[21] The issue of whether the loss of the use of the house and the resulting consequences are "natural disaster damage" under the ECA is essentially an exercise in statutory interpretation, with that phrase at its core. Under s 5(1) of the Interpretation Act 1999 the meaning of an enactment must be ascertained from its text and in light of its purpose. Text and purpose therefore are the key drivers of statutory interpretation, and the meaning apparent from the text should always be cross-checked against purpose.[10] In determining purpose the Court has regard to both the immediate and general legislative context including the social, commercial and other objectives of the enactment.[11] The legislative history can also assist in discerning purpose.

[22] To determine this issue and whether Mallon J was correct, we will consider the ordinary meaning of the words of the statute, the context of those words and the legislative history of the relevant statutory provisions. We will also consider the relevant case law, this being the first case to consider the meaning of the ECA in relation to the present issue.

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9 At [69]–[75].

10 *Commerce Commission v Fonterra Co-operative Group Ltd* [2007] NZSC 36, [2007] 3 NZLR 767 at [22].

11 At [22].

**The Earthquake Commission Act 1993**

[23] The ECA provides in s 18(1) for the insurance of residential property against natural disaster. Section 19 is a similar provision relating to residential land. Section 18 provides:

> **18 Residential buildings**
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> (1) Subject to any regulations made under this Act and to Schedule 3, where a person enters into a contract of fire insurance with an insurance company in respect of any residential building situated in New Zealand, the residential building shall, while that contract is in force, be deemed to be insured under this Act against natural disaster damage for its replacement value …
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> …

[24] There are therefore three requirements for cover:

(a) the property is a residential building situated in New Zealand;

(b) a contract of fire insurance with an insurance company in respect of that building; and

(c) natural disaster damage to the property.

[25] There is no issue that Ms Kraal's home was a residential building, and she had a contract of fire insurance with Allianz. The issue is whether her home suffered natural disaster damage.

[26] Natural disaster damage is defined in s 2 of the ECA as follows:

> **natural disaster damage** means, in relation to property,—
>
> (a) any physical loss or damage to the property occurring as the direct result of a natural disaster; or
>
> (b) any physical loss or damage to the property occurring (whether accidentally or not) as a direct result of measures taken under proper authority to avoid the spreading of, or otherwise to mitigate the consequences of, any natural disaster, but does not include any physical loss or damage to the property for which compensation is payable under any other enactment.

[27] Physical loss or damage is also defined in s 2:

> **physical loss or damage**, in relation to property, includes any physical loss or damage to the property that (in the opinion of the Commission) is imminent as the direct result of a natural disaster which has occurred.

[28] A "natural disaster" as defined in s 2 includes an earthquake, and it is not in issue that there was a natural disaster here.

[29] It can be seen from the definitions of "natural disaster damage" and "physical loss or damage" that natural disaster damage can be of three different types:

(a) physical loss or damage to the property occurring as the direct result of a natural disaster;

(b) physical loss or damage to the property occurring (whether accidentally or not) as a direct result of measures taken under proper authority to avoid the spreading of or otherwise to mitigate the consequences of any natural disaster; or

(c) physical loss or damage to property that (in the opinion of the Commission) is imminent as the direct result of a natural disaster which has occurred.

[30] Under s 18 of the ECA the property is insured for its replacement value up to the statutory maximum. The statutory scheme can be seen as providing a first layer of natural disaster damage cover, which includes earthquake damage. A second or excess layer applies under the private insurance policy taken out by the parties, which also acts as a pre-condition for the operation of the statutory cover. A homeowner is therefore able to insure a property for full replacement value, in excess of the limit in the ECA. However, the private insurance policy need not contain the same terms or provide the same scope of earthquake cover as the ECA. That cover will be governed by the provisions of the relevant insurance policy.

**The ordinary meaning of the text**

[31] It was accepted by Mr Campbell QC for Ms Kraal that the prospect of rock falling and hitting the property was not expected to occur within the next 12 months and was not "imminent" (the third option). He put forward as his primary submission the claim that there was physical loss or damage to the property occurring as a direct result of a natural disaster, and therefore placed primary reliance on part (a) of the definition, although he also relied on part (b). Mr Campbell argued that the addition of the word "physical" was to distinguish between pure economic loss, and loss that had a physical element including loss of possession. He submitted that the addition of "physical" was consistent with "loss" encompassing more than just physical destruction and included deprivation loss, which could have a physical effect.

*The definition at (a)*

[32] We repeat the first ECA definition of "natural disaster damage":

> (a) any physical loss or damage to the property occurring as the direct result of a natural disaster;

[33] It is necessary to consider the adjective "physical", the nouns it qualifies of "loss or damage" and the phrase that follows of "to the property".

[34] In relation to the word "physical", Mr Campbell for the appellants described the proceeding as a claim for "physical deprivation loss", which he argued fell within the phrase "physical loss to the property".

[35] The word "physical" indicates something material or tangible as opposed to mental or spiritual,[12] and ordinarily means "of or concerning the body".[13] The "body" in the context of (a) is the "property". The property is not defined, but must be the building or land that has suffered the loss or damage. In this case it would be the structure and materials of the house.

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12 High Court judgment, above n 2, at [36].

13 See T Deverson and G Kennedy (eds) *The New Zealand Oxford Dictionary* (Oxford University Press, Victoria, 2005) at 852.

[36] Mr Campbell submitted that to be unable to have access to and enjoyment of a house was an event that was a "physical" loss. However, plainly nothing "physical" of significance has happened to the property. The physical deprivation loss Mr Campbell referred to does not relate to any material loss or damage to the body of the property, but a loss to Ms Kraal, who now cannot occupy the property. The earthquakes have given rise to a s 124 notice which stops her and her family from doing so. But neither the earthquakes nor the notice have changed the property in any material or tangible way.

[37] Turning to the word "damage", there was little difference between the parties regarding the interpretations that they put forward. Its ordinary meaning is of harm done to something which impairs its value or usefulness.[14] The word often has a connotation of physical harm, but it can mean emotional or reputational or other non-physical harm. In ordinary parlance it would not be said that a s 124 notice prohibiting occupation has caused "damage" to a property.

[38] The word "loss" has a broader meaning than the word "damage".[15] When used as a noun it is not in its dictionary definition normally associated with the word "to" (although it can be), but is often coupled with "of". It carries as a particular meaning the concept of deprivation of a thing. The word "loss" is broad enough to cover conceptually what has happened to Ms Kraal, in the sense that she had suffered a loss, namely the ability to use her property, and other associated losses. However, the definition refers to loss "to the property", and not loss to the insured person.

[39] We see the word "loss" (which, as we will describe has featured since the War Damage Act 1941 in conjunction with "damage") as having a belts and braces purpose. The long title does not refer to "loss" but only "damage", but there will be cases where "loss" is the more natural word to apply, even when the event is of a physical nature. Thus, if a house or land is swept away in a tsunami or lahar flow it is physically "lost". In our view the word "loss" in the context of the definition can

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14 At 272.
15 At 657.

be seen as adding, to the concept of damage, the concept of total destruction. Both involve a physical event happening to the building.[16]

[40] "Loss" has a broader meaning than "damage", but the word as used in the definition cannot be read without the qualifying adjective "physical". We see the word "loss" in the definition as not broadening the relevant concept to cover any loss suffered to the insured person's property as a consequence of an earthquake which has a physical effect on the person rather than on the property itself. The word "physical" beforehand and the phrase "to the property" afterwards make the definition more prescriptive than that.

[41] The "loss or damage" must be "to the property". The preposition "to" relates to what is reached, approached or touched.[17] In (a) the word "to" follows "loss or damage" and relates to the words "the property". This meaning is emphasised by the adjective "physical" which, as discussed, involves something of or concerning the body. In this definition the body is "the property" or more particularly the materials and structures that constitute the house. Therefore, it is loss or damage that reaches and touches the house and not loss or damage to objects other than the property, such as the insured person or that person's enjoyment of the property, that is covered. It was open to those who drafted the definition if they wished to cover loss in its broadest sense to use the phrase loss "of" the property, and to avoid prescriptive words such as physical. But they did not do so. They specified "physical" loss "to" the property.

[42] Nothing physical of relevance to this claim has happened "to" the property. It has not been hit by a boulder or suffered other injury resulting from destabilisation of the hill. The only reason the house cannot be used is because there are legal prohibitions on its use. Those legal prohibitions in themselves are not physical loss or damage "to" the property.

[43] Therefore, the text of (a) of the definition does not support Ms Kraal's claim. Rather it indicates that a deliberate limit has been placed on the type of loss or

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16 See also *O'Loughlin v Tower Insurance Ltd* [2013] NZHC 670, [2013] 3 NZLR 275 at [52].
17 *The New Zealand Oxford Dictionary*, above n 13, at 1182.

damage that falls within the definition: it must be physical and it must be to the property in the sense of being to the materials and structure of the property. It does not extend to an inability to enjoy the property. The plain text of (a) therefore supports the ECA's definition.

*The definition at (b)*

[44] The text of (b) uses the same clause initiating words that are in (a), defining natural disaster damage as "any physical loss or damage to the property". The above analysis applies to those words. However, the definition in (b) adds to the triggering event of "natural disaster", physical loss or damage to the property that results from measures under proper authority, taken to avoid the spreading of or to mitigate the consequences of natural disaster. Natural disaster remains the trigger, and physical loss or damage to the property remains the loss covered, but the cover for the loss is extended where there has been intervening event between the trigger and the loss. That event is a measure under proper authority taken to mitigate that natural disaster.

[45] In our assessment that measure must still cause physical loss or damage to the property. There has been a measure in this case taken under proper authority to mitigate the consequences of the earthquake, namely a s 124 notice prohibiting persons from occupying houses at risk as a consequence of the earthquake. But that measure has not caused any physical loss or damage to the property. There is no reason why the meaning of "physical loss or damage to the property" should differ between (a) and (b). Thus the claim under (b) fails because there has been no physical effect to the property.

**Purpose of the ECA in context**

*The long title and s 18*

[46] The long title records that the ECA is to provide "insurance of residential property against damage caused by certain natural disasters". The reference is to "damage" rather than "loss". The appellants' loss, which is the deprivation of possession and use and economic loss, does not naturally come within these words.

In ordinary parlance the property has not suffered damage relevant to this claim caused by earthquake.

[47] Further, the emphasis in s 18 is on the property being insured for its "replacement value". That term is defined in s 2 as any costs that would be reasonably incurred in the demolition and removal of debris or replacing or reinstating the building and other related replacement or reinstatement costs. This definition indicates there is insurance for physical damage, rather than for loss of the right to occupy the house.

*The extension to "imminent" damage*

[48] The extended definition of physical loss or damage in s 2 (the history of which is discussed in the next section) also indicates it is physical loss or damage to the property rather than the deprivation of possession that is contemplated by those who drafted the ECA. This extended definition provides that any physical loss or damage, in relation to property, includes loss or damage which is imminent as a direct result of natural disaster. If the approach to interpretation put forward by the appellants was intended, there would have been no need for an extension to loss or damage that was imminent, as such imminent loss would in any event have fallen within the definition of natural disaster damage. Any "imminent" physical loss or damage to property would have meant that the property would, in the ordinary course of events, be subject to a s 124 notice and therefore not useable, meaning there would be a loss in the manner contended by the appellants. It can be assumed that the reason it was thought necessary to extend the definition was because imminent physical loss was not already within the definition.

[49] The fact that the cover was so extended indicates that loss of possession and economic loss of the types that arise in the appellants' claim, where there is no actual physical loss or damage, were not considered by the legislature to be covered. Thus we see the extended definition as strongly supporting the interpretation put forward by the EQC and adopted by Mallon J.

*The legislative history*

[50] It is necessary to traverse the legislative history in some detail as that history gives an indication as to the ambit of natural disaster insurance under the ECA.

[51] The original Act was the War Damage Act 1941 which made provision for the insurance of property against war damage. War damage was defined in s 2 as damage occurring as the direct result of action taken by the enemy, or in combating or repelling the enemy, or damage occurring as a direct result of measures taken under proper authority to avoid the consequences of any such damage. Accidental damage was also defined. There was no reference to "loss", and in the operative clause the Commission was to make good war damage to insured property that had been "destroyed or damaged by war".[18] Thus the legislation began with a focus on property that was destroyed or damaged, rather than on loss of enjoyment of property. However, the War Damage Regulations 1941 interchangeably used "loss" and "destruction".[19]

[52] The 1942 and 1944 Earthquake Damage Emergency Regulations refer only to property being "destroyed" or "damaged",[20] although the regulations go on to state that the Commission will make good "all such loss or damage".

[53] In 1944, the Earthquake and War Damage Act was enacted, thereby extending war damage cover to earthquake damage.[21] The operative provision was in much the same terms as that of the 1941 Act, requiring property to be damaged or destroyed by "earthquake damage" and the Commission to make good "all such loss or damage".[22] Under the interpretation section,[23] damage occurring as the direct result of measures taken under proper authority to avoid the spread of or otherwise mitigate the consequences of such damage was included in the definition. This was a predecessor to (b) in the interpretation section of the ECA.

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18 War Damage Act 1941, s 16(1).
19 War Damage Regulations 1941.
20 Earthquake Damage Emergency Regulations 1942; Earthquake Damage Emergency Regulations 1944, reg 5(1).
21 Earthquake and War Damage Act 1944, s 14(1).
22 Section 16(1).
23 Section 3.

[54] In the 1956 regulations the concepts of "disaster damage", "extraordinary disaster damage" and "landslip damage" were introduced.[24] Following the Abbotsford landslip the Earthquake and War Damage (Land Cover) Regulations 1984 were introduced. Under reg 6 if "the property or any part of it [was] destroyed or damaged by earthquake damage … or landslip damage" the Commission was liable to make good by payment, reinstatement or repair, or by a combination, for such loss or damage.

[55] At the time of the Abbotsford landslip the 1944 Act had been interpreted to mean that the Earthquake and War Damage Commission would not accept responsibility to compensate before damage had proceeded to an advanced state.[25] The Abbotsford Commission of Inquiry noted that this "effectively meant that persons were required to continue living in doomed houses beyond a point when this was desirable".[26]

[56] The regulations that were enacted in 1984 extended the coverage of the 1944 Act in two ways.[27] First, to cover land and retaining walls; and second, to provide cover for "imminent" loss or damage by landslips. The definition of "landslip damage" was extended to include "damage which is imminent as the direct result of landslip if, in the opinion of the Commission, the likely result is total loss of the property concerned".[28]

[57] In 1993 the current Act, the ECA, was enacted after a long gestation, and a major change was to move the responsibility for the cover of commercial property away from the Crown and onto private insurers.[29] In the original draft of the Act, the 1992 Bill, there was no cover for "imminent" loss or damage. The Select Committee received a submission in particular from the Buller District Council relating to a housing area situated underneath an unstable cliff face located at Little Whanganui where the Council had warned (but not directed) residents to leave the area. The

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24 Earthquake and War Damage Regulations 1956, reg 2.

25 *Report of the Commission of Inquiry into the Abbotsford Landslip Disaster* (Wellington, 1980) at [5.6.3.1].

26 At [6.3.1].

27 Earthquake and War Damage Regulations 1984 and Earthquake and War Damage (Land Cover) Regulations 1984.

28 Earthquake and War Damage Regulations 1984, reg 2.

29 (15 December 1992) 532 NZPD 13186.

district plan had been altered to record the area as a rock fall and hazard zone. The Council asked the Government to consider extending coverage to people where the danger of catastrophe was known, but had not occurred, to assist them to relocate.[30]

[58] A further draft of the Bill was prepared. A decision was made in 1993 to move from the words "loss or destruction of, or damage to" to "physical loss or damage to".[31] It can be assumed that Parliament intended the word "damage" to incorporate the notion of destruction thereby rendering the ongoing use of that word unnecessary. However, at this point for the first time the word "physical" was introduced to qualify loss or damage, and the phrase "to the property" was also introduced.

[59] The word "disaster" which had been in the definition was dropped without explanation. Provision for compensation where damage was "imminent" was included, and in the report of the Finance and Expenditure Committee to Parliament discussing compensation for imminent natural disaster damage it was stated:[32]

> The mind of the committee was exercised to no small extent as to the definition of imminent and what the commission or any insurer could be required to protect against.
>
> The recommendation of the committee is that the Bill include a provision to allow the payment of compensation when damage arising from a natural disaster that has occurred is, in the opinion of the commission, imminent. Therefore if a natural disaster has occurred, but in the opinion of the commission further damage is likely to occur, the Earthquake Commission should have the power to pay compensation for the costs incurred in mitigation or prevention of that damage.

[60] The references to "damage arising" and the general tenor of this statement indicate that the concern is imminent physical damage.

[61] In our assessment this history tends to support the interpretation put forward by the EQC rather than the appellants. It indicates an intention to cover events which damage land or the materials or structure of buildings, and to extend that to situations where physical damage is imminent. The changes which led from the

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30 Buller District Council, submission to the Finance and Expenditure Committee *Earthquake Commission Bill* (2 February 1993).

31 Earthquake Commission Bill 1993 (210-2).

32 (20 July 1993) 536 NZPD 16561.

events of the Abbotsford landslip and the threatened slips at Little Whanganui, related to the threat of physical loss rather than loss of possession or economic loss. The word "physical" is an unexplained but clearly intentional addition to the definition of natural disaster damage by Parliament. There is nothing to indicate that contrary to the natural meaning of the words, damage or loss that was not physical and to the body of the property was intended to be covered.

[62] As Mallon J commented, it might have been reasonable for the ECA to provide cover to persons who are forced to leave their properties or not permitted to occupy them because of a natural disaster even when the house and land is undamaged.[33] However, that is not what the ECA says. The context is against that interpretation, and it is not what is indicated by the legislative history.

**Authorities**

[63] The debates and reports that led to the 1993 Act do not rely on or refer to insurance law or practice. Nevertheless it is relevant in interpreting the ECA to consider insurance law or practice, given that it is an Act that provides for insurance of residential property against natural disaster.

[64] There is a considerable body of insurance cases which indicate that physical loss or damage requires a disturbance to the materials or structure of a building or other object.

[65] In the leading decision of *Moore v Evans*,[34] pearls owned by the plaintiff were in transit. World War One broke out, and the occupation of Brussels meant that it was impossible to recover possession. It may have been only communication difficulties that prevented them being returned, and the pearls might have been safe.

[66] The policy was to insure against "loss or damage or misfortune to the before-mentioned property or any part thereof arising from any cause whatsoever". In declining the claim the English Court of Appeal held "there must either be loss of the

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33 High Court judgment, above n 2, at [49].
34 *Moore v Evans* [1917] 1 KB 458 (CA).

property or part of it, or damage or misfortune to it".[35] The decision was upheld on appeal.[36] Mr Campbell sought to distinguish that case on the basis that the Court had noted that the pearls could still be available, whereas Ms Kraal could not get possession of her house in the near future.[37]

[67] In *Pilkington UK Ltd v CGU Insurance plc*[38] defective glass panels in a train terminal had led to the closure of the terminal for a period of time. A claim in respect of the losses resulting from the closure was unsuccessful and the appeal was dismissed. It was held by the English Court of Appeal in relation to a clause which referred to "loss or physical damage to physical property" that the English authorities make clear that:[39]

> … the insured must demonstrate some physical damage caused by the commodity for which purpose a defect or deterioration in the commodity is not itself sufficient *and* that the loss claimed must be a loss resulting from physical loss or damage to physical property of another (or some personal injury).

[68] The Court declined to follow a line of United States of America authority that stood for the proposition that the incorporation of a defective but nonetheless operative item into a building gave rise to physical damage in the ordinary sense. It was held "in English law, 'damage' usually refers to a 'changed physical state'",[40] relying on *Promet Engineering (Singapore) Pte Ltd v Sturge, (The "Nukila")*.[41]

[69] In *Transfield Constructions Pty Ltd v GIO Australia Holdings Pty Ltd*[42] the appellant had constructed grain silos and insured them against physical loss or damage. The fumigation pipes were blocked by grain, with the effect that the fumigants could not escape from the pipes into the silos, and had to be repaired. The question on appeal was whether this constituted physical loss or damage. It was held by the New South Wales Court of Appeal that the fact that the parts were rendered

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35 At 465.
36 *Moore v Evans* [1918] AC 185 (HL).
37 Above n 34, at 465–466.
38 *Pilkington UK Ltd v CGU Insurance plc* [2004] EWCA Civ 23, [2005] 1 All ER 283.
39 At [35].
40 At [50].
41 *Promet Engineering (Singapore) Pte Ltd v Sturge (The "Nukila")* [1997] EWCA Civ 1358, [1997] 2 Lloyd's Rep 146 (CA) at 151.
42 *Transfield Constructions Pty Ltd v GIO Australia Holdings Pty Ltd* [1996] NSWCA 538, (1997) 9 ANZ Insurance Cases 61-336 (NSWCA).

useless by the blockage did not constitute physical damage within the meaning of the policy. Mr Campbell pointed out that the loss was temporary, indeed transient. It was indeed for a shorter period than this period of loss, but it is the reliance of the Court on the absence of physical damage which runs contrary to his argument.

[70] In *Allstate Exploration NI v QBE Insurance (Australia) Ltd*[43] an earthquake caused a rock to fall near a mine. It did not physically damage the insured's property on which the mine was situated, but the rock fall led to a Government order that the mine be closed. The insurance policy covered "physical loss, destruction of or damage to property insured". It was held by the Victorian Court of Appeal that loss in terms of the policy involved the occurrence of physical damage, or at least associated physical damage to an insured's property, and therefore the insurance policy was not engaged.

[71] These cases support an interpretation of "loss or damage" in the context of this area of insurance law that requires physical damage.

[72] This has been the approach taken in recent cases involving the interpretation of house insurance policies arising out of the Christchurch earthquakes, such as *O'Loughlin v Tower Insurance Ltd*[44] and *Rout v Southern Response Earthquake Services Ltd*,[45] which concerned land owned in the "red zone". In that zone the economics and practicalities of ownership were gravely affected by the red zone designation but there was no prohibition on occupying houses. It was held that the red zone designation was not an event that fell within the definition of physical loss or damage.[46]

[73] Mr Campbell has pointed to a distinguishing feature in those cases from the present as there was no prohibition on the occupation of houses in the red zone, and that his argument in this case rests on the physical deprivation of use. We accept that distinction. However, these cases stand for the proposition that loss and damage must be physical loss and damage and that economic loss that does not stem from

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43 *Allstate Exploration NI v QBE Insurance (Australia) Ltd* (2008) 15 ANZ Insurance Cases 61-773 (VCA).

44 Above n 16, at [54].

45 *Rout v Southern Response Earthquake Services Ltd* [2013] NZHC 3262.

46 At [37].

physical damage is not covered by the policies. It is also the approach which has been followed by a Full Court of the High Court in *Earthquake Commission v Insurance Council of New Zealand Inc*. In that case the Court considered land which had changed in level following both the Christchurch earthquakes had suffered "natural disaster damage", for it had physically changed.[47] Following *O'Loughlin v Tower Insurance Ltd*,[48] and Mallon J's decision in this case albeit with one clarification, the Court held the change in land levels constituted "physical damage" and a loss in market value consequent upon that damage was covered.[49] As a direct result of the earthquakes there had been a disturbance to the physical integrity of the land and a change to its physical state, and that was natural disaster damage.[50]

[74] The approach taken in these cases is consistent with the approach supported by the EQC and opposed by Ms Kraal.

[75] Mr Campbell further relied on *Kuwait Airways Corporation v Kuwait Insurance Co SAC*[51] where 15 aeroplanes belonging to the plaintiff were taken into the possession of the invading Iraq Army and flown away. The policy in that case covered "loss or damage to the aircraft …". Rix J held that the aircraft were already lost on 2 August when the airport was occupied, before they were flown away or moved.[52] That day the insured had lost possession and control of their aircraft. Uncertainty rather than unlikelihood of recovery was sufficient.

[76] There are four features which distinguish *Kuwait Airways Corporation v Kuwait Insurance Co SAC* from this case. The first is that the policy covered "loss of … aircraft" as distinct to "loss to". Second, on a plain meaning approach it is easy to see why aircraft that had fallen into the possession of a hostile foreign power who intended to deprive the insured of the use of them and exercise dominion over them, was a "loss of" the aircraft. Further, this was a chattels policy. Given that chattels are moveable and can be lost by the taking of possession and the physical

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47 *Earthquake Commission v Insurance Council of New Zealand Inc* [2014] NZHC 3138 at [79].
48 *O'Loughlin v Tower Insurance Ltd*, above n 16.
49 *Earthquake Commission v Insurance Council of New Zealand Inc*, above n 47, at [73].
50 At [79].
51 *Kuwait Airways Corporation v Kuwait Insurance Co SAC* [1996] 1 Lloyd's Rep 664 (QB).
52 At 686.

moving of them, different considerations apply than to land and buildings. Finally, there was no reference to "physical" loss in the policy.

[77] We conclude that the New Zealand, Australian and English authorities, while not themselves determinative of this issue of statutory interpretation, make clear that in respect of insurance clauses that have similar definitions, the insured must demonstrate some physical damage caused by the triggering event, and that the loss claimed must result from physical loss or damage.

[78] We conclude that the plain meaning, the context, the legislative history, and relevant authorities in New Zealand, Australia and England, all support an interpretation of the ECA that limits the meaning of natural disaster damage to physical damage that arises from a natural disaster, and which is suffered by the land and buildings that are the subject of the claim, or such loss or damage when it results from an authorised measure to mitigate the damage from the disaster, or when such loss or damage is imminent. If the property is a building there must be a physical disturbance to the materials or structure of that building, and the ECA does not extend to a claim for losses arising from an event which has not physically affected the body of the property.

[79] The result is that the EQC succeeds on its primary argument. The claim for a declaration that it was liable to pay the replacement value of the house was rightly dismissed by Mallon J.

**The Allianz claim**

[80] The Allianz policy provided that the policy did not cover loss caused by or arising from earthquakes. Instead, the policy would cover earthquake damage by paying the difference between the cost of repairing or rebuilding their house and the amount the insureds received from the EQC "provided that the Earthquake Commission has accepted liability under the Earthquake Commission Act 1993." Given that the EQC has not paid anything and has not accepted liability, and that it has been held that the EQC is not liable to do so, this condition has not been met and cover is not engaged.

[81] We deal briefly with the arguments that would arise should EQC have been held liable. The policy provides cover for "[a]ccidental physical loss or damage". Even though there are not the re-enforcing considerations of statutory context and legislative history here, for the plain textual reasons we have set out, and relying on the insurance authorities we have referred to, we consider that it is physical loss or damage to the property that is envisaged. Given that the deprivation of use suffered by Ms Kraal was not physical loss or damage in the sense of damage to the body of the material and structures that made up their house, there is no cover. It was Ms Kraal who was affected by the s 124 notice that followed the earthquake damage, not the building.

[82] Given the conclusions that we have reached we do not think it necessary to determine the submission of Mr Thain for Allianz that the earthquakes did not create the risk from rock fall in respect of the house, and that the increase in rock fall risk after the earthquake did not take the level of risk from acceptable to unacceptable.

**Result**

[83] The appeal is dismissed.

[84] Costs would usually follow the event. We received submissions from counsel about the costs options. Mr Campbell argued that this was a test case, and there was a public interest in the determination of the issues. We accept that this was an important case which explored a new issue arising from a disaster of unforeseen and indeed unimaginable proportions. However, the Earthquake Commission through the litigation has treated the legal issue that arose as settled by the clear words of the statute, and never accepted that there was any genuine uncertainty. It never accepted this was a test case. As is clear from our judgment, our analysis is in accord with that assessment, as was the judgment of Mallon J. There is no reason to depart from the usual costs practice.

[85] The appellants must pay the respondents' costs for a standard appeal on a band B basis and usual disbursements. We certify for second counsel for each respondent.

Solicitors:
Wynn Williams, Christchurch for Appellants.
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