THE CCDU BLUEPRINT AND INSURANCE

The Insurance Council of New Zealand's most recent statistics show that just 45% of all commercial claims arising from the Canterbury earthquakes have been settled (despite more than two years having passed since the first earthquake of 4 September 2010). There are, therefore, still a number of commercial claims to be resolved.

The red-zone cordon in the CBD and uncertainty as to what was going to happen with the CBD may have been a factor in the low number of commercial claim settlements. With release of the CCDU Blueprint, insurance issues will again be thrown into stark relief. It is difficult to predict how insurers are going to respond to the Blueprint and its effect on central city building owners' commercial claims. All we can be sure of it that there will again be some complex issues to work through.

Commercial material damage insurance policies are subtly different. The comments below are generic and always, the starting point is the applicable wording.

Reinstatement Insurance Policies

Most commercial policies in Canterbury are reinstatement policies. Generally this means that if the insured is to reinstate (repair or rebuild) an earthquake damaged building, then the insurer will pay for the cost of reinstatement up to the sum insured. If the insured does not reinstate then they will be *"indemnified"* for the loss.

Most policies are silent on what exactly reinstatement involves but most insurers take the view reinstatement requires construction work. Despite this, in our experience, the vast majority of commercial claims are being cash settled. Insurers say this is outside the terms of the policy, but most total loss claims are cash settling for somewhere between indemnity value and reinstatement value. In our experience, to the upper end of this range.

We have heard anecdotally, that the Crown is not looking to purchase or compulsorily acquire properties and the insurance claim. The Crown has its hands full resolving issues with insurers in the residential red-zone and doesn't want to have similar issues in the CBD. This means that insurance claims will need to be resolved and the Crown has indicated it will help property owners.

Equivalent Buildings

Reinstatement under a commercial replacement policy requires replacement with an equivalent building. As a matter of common law, an equivalent building is *"substantially similar"* to that which existed before. Some policies define *"equivalent building"* with an emphasis on the form and structure of the building. Others are referable to its purpose and function.

Under the Blueprint, there are areas with no designation, but still height and other restrictions on the buildings that can be built (for example in the Retail Precinct). Building height in the CBD Core is restricted to seven storeys. If you previously had a taller building and a policy that linked *"equivalent building"* with the structure and form of the building, your insurer might argue replacing it with a seven storey building is not "*reinstatement"* with an *"equivalent building"*. The insurer could argue that, as you are not *"reinstating"*, you are only entitled to be *"indemnified";* that is the indemnity value of the property at the date of the earthquake.

To date, we have found that insurers have been fairly flexible in applying *"equivalent building*" and *"reinstatement"* so we can just hope that this attitude continues and this does not become an issue.

Blueprint Designations

The Crown designation lasts for ten years. During that time, the owner can't do anything to the property to hinder the foreshadowed public works without the written consent of the Canterbury Earthquake Recovery Minister.

If you have a building in an area designated for Crown purchase or compulsory acquisition, the insurer may argue that because of the designation, you are going to sell the property or have it compulsorily acquired, so you will not be reinstating. Therefore, you are only entitled to be indemnified.

If the building is a rebuild or uneconomic to repair then arguably, you are only entitled to the indemnity value of the building. Most commercial policies also allow reinstatement on another site if the building has been destroyed. The downside is that you have to buy the other land. You can use sums paid by the Crown for the designated land to purchase the alternative site, but there may be some hiatus between purchasing another site and receiving Crown payment which will need to be managed/financed.

Alternatively, you could argue that a ten year designation (for non-priority projects, the Stadium for example) is a long time, which may involve a change of Government and/or a change of the Blueprint. In this context, replacement with a *"temporary"* building should suffice.

If the building is damaged but not destroyed, and the insurer won't repair because of the designation, the doctrine of impossibility should apply. It requires the insurer to pay you the cost of repairs. Alternatively, if your policy contains a constructive total loss clause, the damaged building which cannot be repaired due to a *"law"* which includes the designation, is deemed to be destroyed. Therefore, the indemnity value of the whole building may be payable. Most broker wordings contain constructive total loss clauses. Underwriter wordings, less so.

Those with damaged but repairable buildings, in the East Frame for example, may end up receiving the indemnity value of the buildings plus the Crown land compensation, which could should leave them in a reasonable position (depending on the age and condition of the building pre-quake).

Practically, if your building is designated to a precinct that is not a priority, repairs may enable you to re-tenant or reoccupy your building, so that you can generate some rental or business income. This needs to be considered if your insurer suggests designation means repairs are not possible. Be aware though, we have heard anecdotally that the Crown compensation for those who repair or rebuild buildings in designated precincts may be limited to the land value only.

If the property is in the South Frame and/or the Innovation Precinct where some buildings will be allowed, the CCDU can provide written confirmation that there is no obvious reason why the property owner can't reinstate. This can be used for negotiations with the insurer.

In those areas designated for no buildings (the East Frame for example) or for a specific building or buildings (eg the Conference Centre precinct) CCDU letters may not be available, so inability to reinstate could be a problem.

Sale vs. Compulsory Acquisition

At this stage, it seems that owners of designated properties are best served by negotiating with their insurer and the Crown to reach a satisfactory financial outcome for all parties. If the insurer will not pay more than the indemnity value of the destroyed building (or the cost of repairs) the difference between indemnification and the reinstatement sum insured is a loss which should be met by the Crown.

If a Crown designated property owner waits for compulsory acquisition, it will be entitled to compensation under the Canterbury Earthquake Recovery Act. However, this is limited. It does not include losses which are insured or should have been insured or economic and consequential loss. We have heard some suggestion that the loss of the reinstatement benefit of the policy through compulsory acquisition is compensable. We think this loss is probably *"economic loss"* or *"consequential loss"*, so is not compensable under the Canterbury Earthquake Recovery Act.

At this stage, we recommend that if you receive a Property Information Questionnaire take some care in the information provided. All information should be provided *"without prejudice"* (it is, after all, the first step in a negotiation) and do not allow the Crown to have direct contact with your insurer and insurance broker. Information must be controlled.

Finally, take advice before signing a cash settlement agreement with your insurer. Some interesting clauses are finding their way into the insurers' settlement and discharge agreements, which you will want to avoid, if possible.

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