

Reference: 20150125

27 November 2015



**OFFICIAL INFORMATION ACT COMPLAINT – Information relating to EQC**

I refer to your request made under the Official Information Act and received on 14 April 2015. Your request was for:

*“The Earthquake Commission advised the Finance and Expenditure Select Committee, as part of the annual review of EQC’s expenditure and performance in 2013/14, that it had provided Treasury with information on “lessons learned to date about the application of the EQC Act in responding to the Canterbury earthquakes in relation to legislative interpretation, practical application challenges and policy issues identified in the course of the Canterbury response” (answer to question 151 from the Finance and Expenditure Select Committee).*

*Please provide a copy of any briefing reports or analysis which Treasury has done in response to the information which EQC provided on the lessons learned.”*

As you are aware I decided to withhold in full the relevant information under section 9(2)(f)(iv) of the Official Information Act *advice still under consideration – to maintain the current constitutional conventions protecting the confidentiality of advice tendered by Ministers and officials.*

The Ombudsman has advised me that you subsequently lodged a complaint regarding my decision, but has not yet initiated an investigation of that complaint.

I wish to advise you that following the release of the discussion document *New Zealand’s Future Disaster Insurance Scheme*, I now consider that the grounds on which the EQC – related materials were previously withheld, no longer apply.

## Information Being Released

Item	Date	Document Description	Decision
1.	30 August 2013	EQC Act Review: Minor Policy Proposals for Public Consultation	Release in part
2.	5 November 2013	EQC Act Review: Follow-up Reporting on Proposals for Public Consultation	Release in part
3.	28 May 2014	EQC Review: Decisions sought on Feedback from Natural Hazards Expert's Workshop  Attachment: Issues Identified at Natural Hazards Experts' Workshop	Release in part

I have decided to release the documents listed above, subject to information being withheld under the following sections of the Official Information Act, as applicable:

- Personal contact details of officials, under section 9(2)(a) – to protect the privacy of natural persons, including deceased people, and
- Advice still under consideration, section 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by Ministers and officials (FYI the material withheld under this section relates to another project, not the review of the EQC Act).

In making my decision, I have considered the public interest considerations in section 9(1) of the Official Information Act.

Please note that this letter (with your personal details removed) and enclosed documents may be published on the Treasury website.

This now brings to a close your original OIA request and the subsequent Ombudsman complaint.

Yours sincerely

James Beard  
**Manager - International, Financial Markets & Tax Strategy**

# Information Being Released

## TOMB 20150125

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**Treasury Report:** EQC Act Review: Minor Policy Proposals for Public Consultation

<b>Date:</b>	30 August 2013	<b>Report No:</b>	T2013/1556
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**Action Sought**

	<b>Action Sought</b>	<b>Deadline</b>
Minister Responsible for the Earthquake Commission (Hon Gerry Brownlee)	<b>Agree</b> to the recommendations in this report.	None.
Associate Minister of Finance (Hon Dr Jonathan Coleman)	<b>Agree</b> to the recommendations in this report.	None.

**Contact for Telephone Discussion** (if required)

<b>Name</b>	<b>Position</b>	<b>Telephone</b>	<b>1st Contact</b>
Bevan Lye	Senior Analyst	04 917 6063 (wk)	[Withheld under s9(2)(a)]
Steve Cantwell	Project Leader, EQC Act Review	04 917 6144 (wk)	✓

**Actions for the Minister's Office Staff** (if required)

**Return** the signed report to Treasury.

**Enclosure:** No

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30 August 2013

CM-1-3-15-1

**Treasury Report: EQC Act Review: Minor Policy Proposals for Public Consultation**

**Executive Summary**

This report seeks decisions on minor policy proposals for change to the Earthquake Commission Act 1993. If you agree, the proposals in this report will be included in a public discussion document for release in the second half of 2013.

The proposals fall under three general themes:

Theme	Proposals
Increasing certainty & clarity	<ul style="list-style-type: none"> <li>Clarify the types of residential buildings insured by the Act</li> <li>Clarify EQC's liability during a state of emergency</li> </ul>
Enabling greater flexibility	<ul style="list-style-type: none"> <li>Allow for the late notification of damage</li> <li>Specify who can receive the benefits of a claim</li> </ul>
Ensuring the scheme is fair & reasonable	<ul style="list-style-type: none"> <li>Specify when EQC insurance may be cancelled</li> <li>Specify the time at which damage should be valued</li> <li>Specify the grounds on which a claim can be declined</li> <li>Allow for the recovery of payments where a policy is void or cancelled</li> <li>Revision of EQC salvage rights</li> </ul>

Over the past weeks, we have also prepared a draft of the discussion document. We will finalise the draft discussion document after you have reached final decisions on these policy matters, then send the document to you for your consideration.

**Recommended Action**

We recommend that you:

**Proposals to increase certainty and clarity**

- a **agree** the EQC scheme should cover buildings that are used only or mainly for residential purposes (or are intended for such use and occupation)

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

- b **agree** that the EQC scheme should not cover residential buildings that are used, or intended to be used, only or mainly for commercial purposes

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

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- c **agree** that a residential building must comprise or include one or more residential units, and the floor area of the residential unit(s) must constitute 50% or more of the floor area of the building

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- d **agree** that EQC will not insure residential units in a building that is defined, according to the test set out in recommendation c, to be non-residential

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- e **agree** that the natural disaster damage insured by EQC will include damage caused by measures taken under proper authority during a state of emergency declared under the Civil Defence Emergency Management Act 2002 for a period of up to 7 days

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- f **agree** that EQC will have no liability for the indirect effects of the measures referred to in recommendation e

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

**Proposals to enable greater flexibility**

- g **agree** that EQC should be notified of damage within 3 months of the event causing the damage

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- h **agree** that EQC should accept notification of damage and claims for damage made more than 3 months after a natural disaster event unless doing so would prejudice EQC

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- i **agree** that an absolute time limit of 2 years will apply for the notification of damage and claims lodgement

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

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- j **agree** that EQC may settle with insurable interests who are not the insured person

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- k **agree** that EQC may settle with a third party if the person entitled to the benefit of the claim has agreed in writing that the third party should receive the benefit

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

**Proposals to ensure the scheme is fair and reasonable**

- l **agree** that EQC may cancel cover for an individual building and/or associated landholding even when the building is insured by a policy that covers multiple buildings

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- m **agree** that a notice of cancellation of EQC cover in force in relation to any landholding will apply to any new building that is built on that landholding until such time as the notice is removed by EQC

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- n **agree** that the calculation of the value of cash settlement should occur as close as reasonably possible to the date at which the payment is received

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- o **agree** that EQC may decline its portion of a claim that has been declined by a private insurer

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- p **agree** that EQC may decline claims in circumstances where the insured person has not taken reasonable precautions to preserve the insured property from (further) damage

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

- q **agree** that EQC may recover payments already made to a claimant where EQC finds the underlying private fire insurance policy has been voided or cancelled

*Agree/disagree.*  
Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*  
Associate Minister of Finance

**IN-CONFIDENCE**

- r **agree** that EQC may only exercise salvage rights if it is fair and reasonable to do so

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

- s **agree** that EQC may only salvage land if it has paid out the full value of the land

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

- t **agree** to a top-down recovery model in which private insurer losses will be recovered first from any salvage if the limit of EQC insurance is exceeded

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

**Other matters**

- u **agree** to retain offence provisions that enable claimants and insurers to be fined under certain circumstances

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

- v **note** that the Canterbury Earthquakes Royal Commission has recommended amendment to the EQC Act to remove any doubt about the ability of the Commission to disclose information that might affect personal safety, and

- w **agree** that EQC should have the power to disclose information that may affect personal safety

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

Steve Cantwell  
**Project Leader, EQC Act Review**

Hon Gerry Brownlee  
**Minister Responsible for the  
Earthquake Commission**

Hon Dr Jonathan Coleman  
**Associate Minister of Finance**



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## Treasury Report: EQC Act Review: Minor Policy Proposals for Public Consultation

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### Purpose of Report

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1. This report seeks decisions on minor policy proposals for change to the Earthquake Commission Act 1993. If you agree, the proposals in this report will be included in a public discussion document for release in the second half of 2013.

### Policy Approach

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2. The EQC Act would benefit from revision in three main ways:
  - **Increasing certainty and clarity.** We have identified opportunities to reduce complexity and provide clearer guidance in the Act about the purpose of the EQC scheme and the cover it provides.
  - **Enabling greater flexibility.** Where possible, we wish to provide EQC with greater discretion to deal in a more flexible manner with claimants in different circumstances. This should help to reduce the distress and delay experienced by some homeowners in the course of the claims process.
  - **Ensuring the scheme is fair and reasonable.** The scheme should deliver fair outcomes for claimants and enable EQC to deal appropriately with claimants who have abused or neglected their obligations.
3. While it is difficult to quantify the exact costs and benefits of the proposals in dollar terms, the net impact of the proposals on EQC's liability is likely to be small. Collectively, however, these changes should increase the efficiency of EQC's response to future disasters.
4. We expect to identify further issues requiring attention as a result of public submissions on the discussion document, and also during the legislative process. These issues will be covered in future reporting.

### Proposals to Increase Certainty and Clarity

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#### Clarify the types of residential buildings insured by the Act

5. We think it is necessary to re-establish, from a policy perspective, what types of buildings are eligible for EQC cover. The experience in Canterbury has raised questions about what constitutes a dwelling or residential building and is therefore eligible for EQC cover.
6. For example, in Canterbury, the High Court has found that the specific circumstances of six commercial boarding houses mean they are actually dwellings for the purposes of the EQC Act.
7. In our view, the EQC scheme should be clearly limited to buildings that are used only or mainly for private residential purposes (or are intended for such use and occupation). Under this approach, buildings such as rental accommodation, holiday homes for individual households and retirement villages would continue to be insured under the Act.

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8. The scheme should not cover residential buildings that are used, or intended to be used, only or mainly for commercial purposes, such as hotels, boarding-houses, serviced apartments, nursing homes, rental holiday accommodation or campgrounds.
9. The result of this policy position is that some types of properties that are potentially eligible for EQC cover at the moment (such as the six boarding houses covered by the recent High Court decision) will not be eligible for EQC cover in the future.
10. All buildings will need to meet two tests in order to be defined as a residential building:
  - They will need to comprise or include one or more residential units; and
  - The floor area of the residential unit or units will need to constitute 50% or more of the floor area of the building
11. EQC will not insure residential units in a building that is defined, on these tests, to be non-residential.

**Clarify EQC's liability during a state of emergency**

12. Section 109 of the Civil Defence Emergency Management Act 2002 provides for the payment of compensation to property-owners who suffer loss or damage that result from the entry of personnel working under instructions in an emergency situation, but only as a backstop to any insurance cover (including EQC entitlements).
13. The experience of the disaster recovery arrangements in Canterbury – notably the establishment of the red zone cordon, which prevented property-owners from accessing and protecting their property over a long period of time – has generated questions about the cut-off point for EQC's liability in an emergency situation.
14. We propose to clarify that the 'natural disaster damage' insured by EQC will include damage caused by measures taken under proper authority during a state of emergency declared under the Civil Defence Emergency Management Act 2002, for a period of up to 7 days.
15. However, EQC will have no liability for the indirect effects of such measures (e.g. property damage resulting from an inability to enter and secure damaged buildings while a cordon is in force). The costs of such measures will fall upon the homeowner.

**Proposals to Enable Greater Flexibility**

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**Allow for the late notification of damage**

16. The Act currently requires notification of damage within 1 month (extended to 3 months by regulation) and does not provide any discretion for the late notification of damage. This approach is not consistent with the law as it applies to private insurers and has contributed to distress in the context of multiple earthquake events in Canterbury.
17. In Canterbury, some homeowners did not submit claims for every event, because they were confused about their obligations, mistaken about when the damage occurred, too distressed to deal with the paperwork, or simply absent and did not become aware of the damage until later. These homeowners cannot now rectify their omission.

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18. We propose to retain the current timeframe of 3 months to encourage timely notification, but amend the Act to allow EQC to accept claims made after 3 months unless doing so would prejudice EQC to an inequitable extent. This approach is based on the provisions of the Insurance Law Reform Act 1977, which applies to private insurers.
19. We propose to apply an absolute time limit of 2 years for notification to ensure the claims process is not open-ended. (An open-ended notification period would probably be of concern to reinsurers.)

### Specify who can receive the benefits of a claim

20. The Act is unclear about whom EQC should pay when it cash settles a claim. There are two main problems:

- **Insurable interests.** The Act refers variously to the terms 'insured person' and 'insurable interest.' It requires EQC to have regard to the respective insurable interests when settling claims, but is unclear whether payments should be made to persons who are not 'insured persons.'

The term 'insurable interest' is well defined in the insurance industry. A person has an insurable interest in property if loss or damage to that property will cause them to suffer a financial loss or some other kind of loss. We propose to clarify that EQC can, at its discretion, make payments to insurable interests who are not the insured person. This approach will formalise current EQC practice.

- **Deeds of assignment.** The Act is also unclear how EQC should treat a written assignment of the benefits of that claim to another party. This issue is of particular concern when a claimant intends to sell their property before the claim is settled.

There is no obvious reason for the Act to prohibit the assignment of claims. EQC must have due regard to the respective insurable interests when settling a claim, but it should be able to settle a claim with a third party if the person entitled to the benefit of the claim has agreed in writing that the third party should receive the benefit.

This approach will formalise current EQC practice. In cases where a deed of assignment is unclear, EQC will still be able to settle with the original claimant and leave the affected parties to resolve any resulting dispute.

### Proposals to Ensure the Scheme is Fair and Reasonable

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#### Specify when EQC insurance may be cancelled

21. EQC has the power to cancel insurance in situations where damaged property is not replaced or reinstated to its satisfaction. This power protects EQC from the risks associated with properties whose owners fail to carry out repairs adequately (or at all).
22. The Act requires greater clarity about the cancellation of insurance in two situations:
  - **Multiple buildings under a single policy.** If a single policy covers multiple buildings and associated landholdings, the Act should be clear that EQC can cancel cover for inadequately-repaired buildings or land without voiding cover for other buildings or land under the same policy.

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- **New buildings on risky sites.** EQC can decide to cancel cover for a building for site-specific reasons. A problem arises if a new building is constructed on the site, but the site-specific issues are not addressed during construction. In this case, EQC cover may automatically attach to the new building on the purchase of private fire insurance, despite the earlier cancellation.

In this circumstance, the Act needs to be clear that a notice of cancellation in force in relation to any landholding will apply to any new building built on that landholding until such time as the notice is removed by EQC (i.e. when the reasons for cancellation have been addressed).

### Specify the time at which damage should be valued

23. The Act would benefit from greater clarity about the date at which the value of cash settlement should be determined. In a large scale event with a high number of claims, there can be a significant amount of time between the date the damage occurred, the date the damage is assessed, and the date at which the insured person receives payment to repair that damage. The amount that it would cost to fix damage at the event date may have increased (or indeed decreased) by the time a settlement occurs, due to inflation or developments in repair techniques.
24. We propose to amend the Act to reflect the policy that the insured person should receive the amount required to actually reinstate or replace the building, which means that the calculation of the payment should be as close as reasonably possible to the date at which the payment is received. The exact wording of the amendment will need to provide sufficient flexibility to achieve a fair outcome reflecting the policy intent.

### Specify the grounds on which a claim can be declined

25. The Act allows EQC to decline claims in certain circumstances. We think there are two circumstances in which the power to decline claims requires clarification:
  - **Claims declined by a private insurer.** For consistency's sake, EQC should have the ability (but not be required) to decline its portion of claims that have already been declined by a private insurer. Such claims are usually declined due to fraud, non-disclosure or a change of building use.
  - **Failure to take reasonable precautions.** The Act requires insured persons to take all 'reasonable steps' to preserve their property from (further) damage. The Act could be clearer about EQC's ability to decline claims when an insured person fails to fulfil this obligation. EQC will also need to provide greater guidance about what will constitute 'reasonable steps,' so homeowners can be aware of their obligations.

### Allow for the recovery of payments where a policy has been voided or cancelled

26. EQC does not have a direct relationship with homeowners outside of the claims handling process. As a result, EQC payments are sometimes made to claimants before EQC becomes aware that the underlying private fire insurance policy is subsequently cancelled or void (e.g. due to the discovery of fraud, non-disclosure or a change of building use).
27. We have proposed separately that claims should be notified and lodged via the claimants' private insurer (T2013/1128 refers). This will reduce the potential for such mistakes to occur in the future because the private insurer will need to verify claims before passing them on to EQC.

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28. Nevertheless, recognising that mistakes may still occur, and that private insurers may also act after EQC has concluded its assessment and settlement process, the Act should allow EQC to recover payments already made to a claimant where EQC subsequently finds that the original private fire insurance policy has been voided or cancelled.

### Changes to salvage rights

29. The Act offers EQC salvage rights over damaged property. These salvage rights are rarely – if ever – exercised, but they serve as a useful deterrent to fraud. (This is because the insured person must be ready to hand over the damaged property to EQC for disposal.) Nevertheless, EQC's salvage rights do not appear to be fair and reasonable in all respects. We have identified three main problems.
- **Triggering mechanism.** The Act suggests that EQC may exercise salvage rights every time damage occurs, regardless of the severity of the damage. This gives EQC an inappropriately expansive right to salvage. We propose that EQC should only be allowed to exercise salvage rights where it is fair and reasonable to do so, taking into account matters such as the nature of the damage and the value of the insurance payment relative to the value of the damaged property.
  - **Salvage of land.** EQC's ability to salvage land could be usefully clarified. EQC should only have the right to salvage the land if it pays out the full value of the land. It is not fair or reasonable for EQC to exercise salvage rights if the claimant has not received a payment for the full value of their land.
  - **Private insurers' salvage interests.** The Act does not anticipate the salvage interests of private insurers. We propose to remove the current uncertainty regarding private insurers' salvage interests by introducing a 'top-down' recovery model in which private insurer losses will be recovered first from any salvage if the limit of EQC insurance is exceeded. The balance of any remaining salvage value would then go to EQC.

### Other Matters

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30. The EQC Act includes offence provisions that enable insurers and claimants to be prosecuted and fined in certain circumstances. The value of the fines is relatively small. EQC informs us that the provisions have never been used, but sees value in retaining them to deter inappropriate behaviour by claimants and insurers. On this basis, we propose to retain the offence provisions, but increase the amount of the fines in proportion with the new EQC building exposure.
31. The Canterbury Earthquakes Royal Commission has recommended amendment to the EQC Act to remove any doubt about the ability of the Commission to disclose information that might affect personal safety. The Commission has also suggested specific wording for the amendment. We recommend you support the intent of the proposal, although the wording may require change during the legislative process.

### Next Steps

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32. Over the past weeks, we have also prepared a draft of the discussion document. We will finalise the draft discussion document after you have reached final decisions on these policy matters, then send the document to you for your consideration.

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## Treasury Report: EQC Act Review: Follow-up Reporting on Proposals for Public Consultation

<b>Date:</b>	5 November 2013	<b>Report No:</b>	T2013/2594
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### Action Sought

	Action Sought	Deadline
Minister responsible for the Earthquake Commission (Hon Gerry Brownlee)	<b>Agree</b> to the recommendations in this report.	Joint Ministers are scheduled to discuss this report with officials at 3.00pm, Monday 11 November.
Associate Minister of Finance (Hon Dr Jonathan Coleman)	<b>Agree</b> to the recommendations in this report.	Joint Ministers are scheduled to discuss this report with officials at 3.00pm, Monday 11 November.

### Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Steve Cantwell	Principal Advisor	04 917 6144 (wk)	[Withheld under s9(2)(a)] ✓
Fiona Ross	Manager, Financial Markets and International	04 917 6165 (wk)	

### Actions for the Minister's Office Staff (if required)

**Return** the signed report to Treasury.

**Enclosure:** No



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5 November 2013

CM-1-3-15-1

**Treasury Report: EQC Act Review: Follow-up Reporting on  
Proposals for Public Consultation**

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**Executive Summary**

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You met officials on 16 September to discuss two Treasury Reports that recommended policy proposals for public consultation regarding reform of the EQC scheme. You agreed with most of the recommendations in those reports, and asked for more reporting on some others. The outstanding issues are:

- *EQC cover for non-residential (commercial) land:* You asked for more advice on the option of EQC cover being available for non-residential (commercial) land.
- *Definition of 'residential building':* You expressed concern that the proposed 50% rule (that a building is not a residential building unless more than 50% of the building floor area is comprised of household units) may cause difficulties for mixed-use developments. You also asked for more advice on how the boundary would be drawn between different building uses (e.g. motel units (not currently covered by EQC) versus units in retirement villages (which are covered)).
- *Clarifying EQC's liability for damage caused by the exercise of powers during a state of emergency for indirect damage* (e.g. due to the exercise of emergency powers to maintain a safety/ security cordon)
- *EQC be able to decline claims that are declined by the policy owner's private insurer:* You expressed concern that this may result in EQC declining claims that had been inappropriately declined by a private insurer.

You also outlined your preferred process from here, namely that you make decisions on the above issues, and then take a noting paper to Cabinet advising of your intention to consult other parliamentary parties on the key elements of the proposed policy changes and, following that consultation, bring a draft Discussion Document back to Cabinet for approval to release.

This paper provides further advice on the above four outstanding policy issues and outlines a potential timeline to enact a new EQC Act that reflects that process.

**EQC cover for non-residential (commercial) land-** we strongly advise against extending land cover beyond the land cover associated with insured residential buildings. Reasons include the large fiscal and policy risks from diluting the EQC scheme's focus on insured residential property, the lack of business interest, and the potential to delay recovery.

**Definition of residential building-** we seek confirmation of previous decisions that EQC building cover only be available to 'household units' in buildings that are predominantly residential. This is a continuation of existing policy intent, although ambiguities in the existing legislation mean this has not always been achieved.

We seek your agreement to a 50% of floor area test to determine whether a building is predominantly residential. Under this approach, if a building is a 'residential building' and EQC levies have been paid in respect of the building, the building and associated 'residential land' will be covered by EQC. Household units in a non-residential building will not need to be covered by EQC as the entire building would be insured on a normal commercial basis.

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Ministers also asked how the boundary would be drawn between different building uses – for instance, it was observed that “a retirement village looks a lot like a motel”.

Individuals’ living arrangements vary hugely and judgements will always need to be made on where to draw a line between residential (covered by EQC) and non-residential (not covered) accommodation.

Motel units operated in the normal manner (i.e. shorter-term accommodation for travellers) would not be ‘household units’ (to be defined in the EQC Act). In contrast, units in a retirement village used as the permanent home of village residents would be household units for the purpose of the EQC Act. The clearer definition of a residential building proposed in *EQC Act Review: Minor Policy Proposals for Public Consultation* along with associated definitions of ‘household unit’ and specified inclusions and exclusions aims to provide much greater clarity and guidance.

**Clarifying EQC’s liability for damage caused by the exercise of powers during a state of emergency-** in response to Ministers’ concerns that insured property owners should not face losses associated with the deterioration of property that cannot be accessed/protected due to security cordons, we recommend extending EQC cover to include damage by natural causes during the state of emergency. To protect the Crown’s interest the EQC Act requirement that property owners take all reasonable steps to minimise consequential damage to their property is retained.

**EQC be able to decline claims that are declined by the policy owner’s private insurer-** in response to Ministers’ concerns we have narrowed this proposal and now recommend that EQC be able to consider declining its portion of a claim if that claim has been declined by a private insurer on grounds available to EQC to decline a claim.

**Timeline and process-** we outline for discussion a process that would see you taking a paper to Cabinet in February next year, followed by consultation with other Parliamentary parties, and release of a public discussion document in mid-2014.

## Recommended Action

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We recommend that you:

### EQC Land Cover

- a **confirm** that EQC land cover should continue to be limited to only residential land on which there is a residential building covered by EQC;

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

### Definition of Residential Building

- b **confirm** that EQC building cover should continue to be limited to buildings that are used only or mainly for residential purposes (or are intended for such use and occupation);

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance



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- c **confirm** that the EQC scheme should not cover household units in buildings that are used, or intended to be used, only or mainly for non-residential purposes;

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

- d **note** that insurance cover for household units in buildings that are used mainly for non-residential purposes is usually provided via the insurance cover on the entire non-residential building;

- e **agree** that, for any building to qualify as a 'residential building' and to be eligible for EQC cover, household units must constitute 50% or more of the floor area of the building;

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

- f **note** that agreeing to recommendation (e) would mean that EQC would not insure household units in a building that, according to the test set out in that recommendation, is not a 'residential building';

**EQC Liability as a result of Actions Taken during State of Emergency**

- g **note** that in Treasury Report T2013/1556 you agreed that the natural disaster damage insured by EQC will include damage caused directly by measures taken under proper authority during a state of emergency declared under the Civil Defence Emergency Management Act 2002 for a period of up to 7 days;

- h **agree** that natural disaster damage insured by EQC will include damage arising from natural causes (eg, rainfall) that is caused indirectly by measures taken under proper authority during the full extent of a state of emergency declared under the Civil Defence Emergency Management Act 2002 (ie, without the 7 day limitation);

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

**Power to Decline Claims Declined by Private Insurers**

- i **agree** that EQC be able to consider declining its portion of a claim if that claim has been declined by a private insurer on grounds available to EQC to decline a claim, and

*Agree/disagree.*

Minister Responsible for the  
Earthquake Commission

*Agree/disagree.*

Associate Minister of Finance

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**Future Timelines and Process**

- j **discuss** the indicative timeline for completing the EQC Review in the *Next Steps* section of this report.

Fiona Ross  
**Manager, Financial Markets**

Hon Gerry Brownlee  
**Minister of Transport**

Hon Dr Jonathan Coleman  
**Associate Minister of Finance**

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OFFICIAL INFORMATION ACT

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## Treasury Report: EQC Act Review: Follow-up Reporting on Proposals for Public Consultation

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### Purpose of Report

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1. This report addresses questions raised by Ministers when we met on 16 September to discuss two Treasury Reports that recommended a package of policy proposals for public consultation regarding reform of the EQC scheme.

### Issues Requiring Further Reporting

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2. You met officials on 17 September to discuss two Treasury Reports that recommended policy proposals for public consultation regarding reform of the EQC scheme. Those reports were *EQC Act Review: Minor Policy Proposals for Public Consultation* (T2013/1556) and *EQC Act Review: confirmation of Core Policy Proposals for Public Consultation* (T2013/2074). You agreed with most of the recommendations in those reports, and asked for more reporting on others. The outstanding issues are:
  - *EQC Cover for non-residential (commercial) land:* You asked for more advice on the option of EQC cover being available for non-residential (commercial) land.
  - *Definition of 'residential building':* You expressed concern about the proposed 50% rule (that a building is not a residential building unless more than 50% of the building floor area is comprised of household units) may cause difficulties for mixed-use developments. You also asked for more advice on how the boundary would be drawn between different building uses (e.g. motel units (not currently covered by EQC) versus units in retirement villages (which are covered)).
  - *Clarifying EQC's liability for damage caused by the exercise of powers during a state of emergency for indirect damage* (e.g. due to the exercise of emergency powers to maintain a safety/ security cordon)
  - *EQC be able to decline claims that are declined by the policy owner's private insurer.*
3. You also outlined your preferred process from here, namely that you make decisions on the above issues, and then take a noting paper to Cabinet advising of your intention to consult other Parliamentary parties on the key elements of the proposed policy changes and, following that consultation, bring a draft Discussion Document back to Cabinet for approval to release. This paper also outlines a potential timeline to enact a new EQC Act that reflects that process.

### ***EQC Cover for Non-residential (Commercial) Land***

4. You asked for more advice on the option of EQC cover being available for non-residential (commercial) land.
5. Your concern appeared to be related to commercial, non-residential and uninsured residential properties within the residential 'red zone' of greater Christchurch and the Crown decision to offer only 50% of the land value, compared with 100% of land and building value offered to insured residential property owners.

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6. We strongly advise against extending the EQC scheme to cover commercial and any other non-residential land. Difficulties we see in extending cover to non-residential land include:

- Business has not sought compensation for property losses outside the residential red zone offer, nor lobbied to extend the EQC scheme to non-residential property. Therefore we see no strong political economy rationale to extend the scheme.
- Extending EQC cover to non-residential land would import into non-residential insurance claims the difficulties experienced between EQC and insurers regarding the boundary between residential land and residential building cover. This is likely to slow the processing of non-residential insurance claims and reduce the pace of recovery.
- Extending EQC cover would increase risk to the Crown (in particular by exposing EQC to existing non-residential developments on vulnerable land). Shedding non-residential property risks was a key motivation for the removal of non-residential property from the scheme in 1993. Built-on residential land (i.e. land potentially covered by EQC) accounts for about half the value of all New Zealand land.

**Table 1: August 2012 QVNZ Land Values by Land Use Category**

Land Use	Value of Land (\$)
Residential (built upon)	\$290b
Residential (vacant)	\$18b
Other (incl. commercial, industrial, rural and religious)	\$282b
<b>Total</b>	<b>\$590b</b>

- The addition of more land-only risk will complicate EQC's reinsurance arrangements. We have not sought market feedback on this, but would anticipate that reinsurers would likely seek to exclude land-only cover from the reinsurance contracts, leaving all or most of this risk with the Crown.
  - Lastly, if non-residential land is covered by EQC, a decision would be required on what to exclude (eg, land used by not-for-profits, industrial and/or rural landholders). Pressure to extend the scheme further may be hard to resist, given the definitional challenges and apparent policy arbitrariness in favouring commercial over other forms of non-residential land use.
7. As your concerns relate to the residential red zone offer rather than the EQC scheme, we think the best solution to the issues raised by Ministers is to reflect the lessons learned from the residential red zone offer in any future similar offers, rather than to extend the EQC scheme to include any form of non-residential land.

***Definition of Residential Building***

***Determining if a building is predominantly residential***

8. The current policy intent of the EQC Act is for EQC to cover only buildings that are used predominantly for private residential purposes and all other buildings to be entirely privately insured.
9. However the current definition has failed to deliver against that policy intention. The current definition of residential building reads, in part:

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***residential building means—***

*(a) any building, or part of a building, or other structure (whether or not fixed to land or to another building, part, or structure) in New Zealand which comprises or includes 1 or more dwellings, if the area of the dwelling or dwellings constitutes 50% or more of the total area of the building, part, or structure*

10. The current definition creates a raft of interpretation difficulties. These include:
  - the different meanings of “building, part, or structure”.
  - The meaning of a “part of the building” – a floor, part of a floor?
  - Whether the word “structure” adds anything to the definition.
11. This has created issues such as a single household unit in a large non-residential building (e.g., a penthouse on top of a multi-story office/retail building) being covered, creating complexities for both building and land cover.
12. A point not made in the last report is that the proposed change to the 50% rule is intended to better reflect the current policy intent that EQC only cover buildings that are used predominantly for private residential purposes.
13. The proposal is to retain the policy intent of the current 50% rule, but with a simpler, more certain test. For example, by removing the reference to ‘part’ of a building it immediately becomes much clearer when a building is a ‘residential building’ by virtue percentage of the floor area comprised of household units.
14. When we last met Ministers expressed concern that the proposed rule (that a building is a residential building if more than 50% of the floor area is comprised of household units) Ministers expressed concerns that qualifying as a residential building would entitle the entire building to land cover. Ministers were also concerned that the rule may cause difficulties for mixed-use developments, potentially discouraging mixed-use developments with less than 50% household units that are appearing as part of Auckland’s urban intensification.

***Land Cover for Mixed-use Buildings***

15. Under the proposed rules, if a building is more than 50% household units, the entire building is considered “predominantly residential” and so entitled to land cover for the whole building. As discussed below under *Other Options*, options involving partial land cover for mixed-use buildings open up a raft of policy and administrative complexities. Therefore we recommend an all or nothing approach to land cover.

***Impact on Mixed-use Buildings that are not Predominantly Residential***

16. Regarding mixed-use developments, the proposed approach is unlikely to discourage mixed-use developments in Auckland. Under current market conditions, Auckland disaster (i.e. volcano) risk is relatively inexpensive. Therefore the non-coverage of this risk by EQC should have little impact on insurer pricing in Auckland.
17. While the 50% rule may have some impact at the margin in some other regions, particularly Wellington and Christchurch, the incentive on property developers to be driven by a 50% rule in the EQC Act will be relatively minor compared to the key driver of overall commercial yield.
18. Non-residential insurance is still available for any mixed use development that comprises less than 50% household units by floor area. Although these policies do not explicitly include separate land cover, in practice any necessary land works are carried

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out as part of the process of reinstating or replacing a damaged building, which is the owners' key concern. Commercial insurance is typically managed by a broker who helps the owner make informed choices regarding appropriate insurance cover.

19. EQC claims data from Canterbury suggests mixed-use buildings contain a small fraction (about 3%) of multi-unit dwellings.

**Table 2: Multi-unit buildings that have suffered earthquake damage in Canterbury**

Dwelling Type	No. of buildings <sup>1</sup>	% of total
Semi-Detached and Terraced Houses	7030	67
Apartment Buildings and Body Corporates	3043	29
Mixed Use (residential and commercial in a single building)	351	3
Rest Homes	111	1
<b>Total</b>	<b>10,535</b>	<b>100</b>

*Other Options*

20. Although technical aspects of the current 50% rule have created uncertainty, stakeholders have not expressed concern with the principle that EQC cover be limited to buildings that are predominantly residential. Therefore we have not closely examined other options.
21. If Ministers wished to pursue other options, we think that the least problematic alternative would be to provide building-only cover on a household unit basis to buildings that are less than 50% residential. For example, if a commercial high-rise had two penthouses, the building would be entitled to EQC cover for two times the household unit building dollar cap (if EQC levies had been paid on those two units).
22. However the building would not be entitled to land cover unless it was predominantly residential. Land cover is too complex to apportion between residential and non-residential use (for instance, with the penthouse example, is EQC required to reinstate land sufficient to enable foundations capable of supporting the original high-rise to be reinstated, so the penthouse can be rebuilt? Or, if the building ground floorplate is larger than the floor area covered by household units, how is land cover calculated?).
23. This option would soften the impact of the 50% test, at the price of reducing the policy clarity of insuring only predominantly residential buildings. It would introduce a new policy intention to cover residences in predominantly non-residential buildings. That could become a pressure-point for further extensions to the scheme.

*What Forms of Accommodation Should EQC cover?*

24. Ministers also asked where to draw the boundary as to what was a residence – for instance a retirement village looks a lot like a motel.
25. Individuals' living arrangements vary hugely and judgements will always need to be made on where to draw a line between residential (covered by EQC) and non-residential (not covered) accommodation.

<sup>1</sup> EQC has building numbers but not dwelling numbers for each category of multi-unit building.



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26. Motel units operated in the normal manner (i.e. shorter-term accommodation for travellers) would not be 'household units' (to be defined in the EQC Act). In contrast, units in a retirement village used as the permanent home of village residents would be household units for the purpose of the EQC Act. The clearer definition of a residential building proposed in *EQC Act Review: Minor Policy Proposals for Public Consultation* (T2013/1556) along with associated definitions of 'household unit' and specified inclusions and exclusions aims to provide much greater clarity and guidance.

***Clarifying EQC's liability during a state of emergency***

27. The experience of the disaster recovery arrangements in Canterbury – notably the establishment of the red zone security cordon within the 'four avenues' area of central Christchurch, which prevented property-owners from accessing and protecting their property over a long period and well beyond the end of the declared state of emergency – has generated questions about the cut-off point for EQC and wider Crown liabilities where Crown powers are being exercised post-disaster.
28. In T2013/1556 we proposed to clarify that the 'natural disaster damage' insured by EQC will include damage caused directly by measures taken under proper authority during a state of emergency declared under the Civil Defence Emergency Management Act 2002, for a period of up to 7 days, regardless of how long the declared state of emergency was in force. This would mean that EQC would have no liability for the indirect effects of such measures (e.g. property damaged by rainfall due to the owner's inability to enter and secure or otherwise protect property while a security cordon is in force).
29. When we discussed this Ministers disagreed with this outcome. Therefore we recommend that natural disaster damage insured by EQC will also include damage arising from natural causes (eg, rainfall) that is caused indirectly by measures taken under proper authority during the full extent of a state of emergency declared under the Civil Defence Emergency Management Act 2002 (ie, without the 7 day limitation). This would mean that insured property owners will be able to claim for water damage or other deterioration due to natural causes as a result of being prevented by the exercise of Crown powers to take steps to prevent or reduce the damage.
30. We have made enquiries with several agencies (EQC, CERA, DIA) and been unable to find any information on the potential costs of this change.
31. In the case of Canterbury, the state of emergency following the 22 February 2011 earthquake ended on 30 April 2011. Enforcement of cordons after the end of the state of emergency was used CERA's powers. If it had been in effect at the time, the recommended approach would have meant that EQC liability for indirect costs would have ceased on 30 April 2011.
32. Should a future government wish to protect homeowners beyond that point a state of emergency declared under the Civil Defence Emergency Management Act 2002 ends, it would need to be via a mechanism that gave reinsurers confidence the government wasn't legislating extra liability onto them. The most direct way to do this would be outside of the EQC scheme. If a future government takes measures that impede the ability of homeowners to mitigate damage (e.g., by denying access to their homes) beyond the expiration of the state of emergency (either through an agency like CERA, or some other mechanism) it may also allow for compensation outside the EQC scheme of homeowners for damage arising from natural causes (eg, rainfall) that is caused indirectly by those measures.
33. The current requirement that the insured person take "all reasonable steps to preserve the insured property from further natural disaster damage" would be retained. So the extension of the cover for indirect damage from natural causes

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would not reduce the property owner's obligation to take all reasonable steps to reduce that damage (but recognises that, if a cordon is in place, property owners would probably not be able to carry out any such reasonable steps).

***Enable EQC to decline claims that had been declined by the policy owner's private insurer***

34. In T2013/1556 we proposed that EQC should have the ability (but not be required) to decline its portion of claims that have already been declined by a private insurer. Such claims are usually declined due to fraud, non-disclosure or a change of building use.
35. Ministers requested more information on this proposal. The concern was that this change could result in EQC declining claims that have been inappropriately declined by the private insurer.
36. This proposal will not *require* EQC to decline claims that have been declined by a private insurer. It would provide EQC with a discretion that it currently does not have. It is not intended that EQC uses this power in every situation where a private insurer declines a claim but rather in situations where:
- a fraud takes place that renders an insurance contract void;
  - there is pre-contract non-disclosure by the insured person; and/or
  - there is a change of building use prior to the natural disaster such that it was not actually a residential building at the time the damage occurred.
37. This is to strengthen provisions in the EQC Act regarding the denial of claims, which reads in part that a claim may be declined by EQC if:
- *"there is or has been on the part of the insured person (whether to the Commission or its agents or to the insurance company concerned)—*
    - (i) any wilful and material misdescription of any of the property, or of any building or land in or on which the property is situated; or*
    - (ii) any misrepresentation as to any matter material for the purpose of estimating the value of the property; or*
  - *the claim is in any respect fraudulent;"*
38. Rather than a blanket ability to decline claims declined by a private insurer, we now recommend that EQC be able to consider declining claims that are declined by private insurers on grounds that EQC is also able to decline claims (these include fraud, misrepresentation and misinformation as outlined above).
39. If Ministers confirm that EQC building cover should be limited to residential buildings, officials intend as part of the drafting process to add to the above existing grounds for declining claim one further ground, namely that the building was not a residential building at the time the damage was incurred. This would reflect current and proposed future policy and would clarify the intended treatment in situations where a building has been converted from its residential use and retained EQC cover by virtue of a fire insurance policy continuing in force simply because the private insurer was not advised of the change in use.



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Next Steps

40. At our last meeting Ministers indicated that from here you would like to take a paper to Cabinet outlining the key elements of the reform package and advising of your intention to consult other Parliamentary parties on the package, and, following that consultation, take a draft Discussion Document to Cabinet seeking permission for its public release.
41. There is insufficient time to get a paper to Cabinet before Christmas using normal processes:

Output	Timing
Officials and Ministers meet to discuss this paper and make final decisions.	11 November
Officials draft Cabinet paper on consultation with Parliamentary parties, test with OEGI and submit to joint Ministers for consideration and signature, and Ministers submit Cabinet paper to Cabinet Office	14 November
EGL Cabinet Committee	20 November (no EGL on the 27th)
Cabinet consideration of paper (last Cabinet meeting of the year is 9 December. Officials are usually directed to avoid this unless absolutely necessary)	2 December

A more feasible indicative timeline would be:

Output	Timing
Officials and Ministers meet to discuss this paper and make final decisions. Officials draft Cabinet paper on consultation with Parliamentary parties, test with OEGI and submit to joint Ministers for consideration and signature.	By end November
Cabinet paper submitted to Cabinet Office	Jan-Feb 2014
First EGL Cabinet Committee of 2014	Likely early Feb 2014
Cabinet consideration of paper (last Cabinet meeting of the year is 9 December, officials are usually asked to avoid this unless absolutely necessary)	Feb 2014
Consultation with Parliamentary parties	Feb-March 2014
Cabinet paper on the outcome of those consultations, a preferred set of proposals for public consultation, and a draft Discussion Document for approval for release.	April 2014
Release of Discussion document	May 2014
Public consultation	May-June 2014
Report-back to responsible Ministers on submissions	July 2014
Report-back to Cabinet on submissions and final policy proposals	August 2014
PCO drafts bill to replace existing EQC Act.	August-October 2014
Draft Bill approved by LEG	October 2014
Bill introduced to the House	Early 2015
Bill enacted	Mid-2015

42. This assumes that the Cabinet and consultation processes do not generate any significant new policy work or extended consideration.
43. We would like to discuss these timings with you when we meet.

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**Treasury Report:** EQC Review: Decisions Sought on Feedback from  
Natural Hazards Experts' Workshop

<b>Date:</b>	28 May 2014	<b>Report No:</b>	T2014/911
		<b>File Number:</b>	CM-1-3-15-1

**Action Sought**

	<b>Action Sought</b>	<b>Deadline</b>
Minister Responsible for the Earthquake Commission (Hon Gerry Brownlee)	<b>Read</b> before next meeting with officials on the EQC Review.	4.30pm Thursday 29 May
Associate Minister of Finance (Hon Dr Jonathan Coleman)	<b>Read</b> before next meeting with officials on the EQC Review.	4.30pm Thursday 29 May

**Contact for Telephone Discussion** (if required)

<b>Name</b>	<b>Position</b>	<b>Telephone</b>	<b>1st Contact</b>
Steve Cantwell	Principal Advisor, Financial Markets	04 917 6144 (wk)	[Withheld under s9(2)(a)] ✓
Anna Everton	Acting Manager/Team Leader, Financial Markets	04 917 6976 (wk)	

**Actions for the Minister's Office Staff** (if required)

**Return** the signed report to Treasury.

**Enclosure:** Yes (attached)

[EQC Review: Table for Ministers of Issues from EQC Experts workshop, 26 March \(Treasury:2907039\)](#) [Add to worklist](#)

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## **Treasury Report: EQC Review: Decisions Sought on Feedback from Natural Hazards Experts' Workshop**

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### **Purpose**

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The purpose of this report is to seek decisions from you on issues raised at the recent experts' workshop regarding the proposed reforms to the EQC scheme.

### **Background**

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At a meeting with officials on 29 January to discuss a draft Cabinet paper on the EQC Review, you asked for an assessment from relevant experts of predictable future claims complexities regarding the scheme. Your thinking appeared to be that while natural disasters have an inherently unpredictable element, working through the damage mechanisms and interactions now may identify some claims complexities that can be addressed in the legislation supporting the reformed EQC scheme.

In response to this request, EQC hosted, with support from Treasury, a day-long workshop of independent experts on 26 March to consider these issues. The independent experts included:

- Geological and Nuclear Science (GNS): Kelvin Berryman, Gill Jolly and Chris Massey
- National Institute of Water and Atmospheric Science (NIWA): Rob Bell
- Tonkin and Taylor (Geotechnical and other engineering expertise): Nick Rogers, John Leeves, Marje Russ, Shamus Wallace, Kate Williams.

### **Key Issues Raised**

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The issues raised by participants, and officials' recommended responses, are summarised in the annexed table. Those with potentially significant policy implications include:

#### **Loss of EQC Cover Following or in Anticipation of a Natural Disaster**

- Payout of a total loss insurance claim on a building leaves the associated land without EQC land cover until fire insurance is issued on a residential building rebuilt on the site (we recommend no change);

#### **EQC Scheme Coverage and Repair Powers**

- Enhancing EQC's ability to perform area-wide land repairs (we recommend support);
- Potential for a period of extended volcanic unrest to cause private insurers to exit from cover in the area, or to trigger the issue of section 124 notices on affected properties (we recommend no change);
- EQC's treatment of gradual deterioration damage (we recommend excluding this damage);

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- Limiting “physical damage” to exclude temporary effects, or changes in risk profile, such as changes in flood risk (we recommend excluding this damage);

**Connections to wider government risk management and response**

- EQC’s role in whole-of-government recovery needs to be considered alongside other recovery legislation and broader recovery issues (we recommend that the new Act facilitate this);
- Amending the RMA to permit EQC to carry out emergency works without resource consent (we recommend no change and refer the issue to the Ministry for the Environment, who are the responsible department for the RMA).

We are scheduled to meet you at 4.30p.m. on 29 May for a workshop on current design choices. If time permits we could discuss this paper with you then.

**Consultation**

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The interdepartmental governance group (Treasury, EQC, the Reserve Bank, MBIE and independent expert Bevan Killick) have been consulted on this paper.

**Recommended Action**

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We recommend that you:

**Loss of EQC Cover Following or in Anticipation of a Natural Disaster**

**Note** that payout of a total loss insurance claim on a building leaves the associated land without EQC land cover until fire insurance is issued on a residential building rebuilt on the site

**Confirm** that land cover continue to only be available to residential buildings with a qualifying fire insurance policy in place

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Note** that ongoing volcanic unrest could lead to private insurers cancelling fire insurance cover for an area, leaving that area with no EQC cover

**Agree** to retain homeowners’ existing ability under the EQC Act to buy EQC cover directly from EQC

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Note** that ongoing volcanic unrest could result in notices being issued under s.124 of the Building Act preventing homeowners from entering badly affected properties

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**EQC Scheme Coverage and Repair Powers**

**Agree** that the Bill include provisions to facilitate area-wide land repairs, where that is the most economical solution to meet EQC's repair obligations

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Agree** that the EQC scheme only cover damage that is sustained or permanent

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Agree** that changes in risk profile be an insurable loss only if as a result there is the prospect of an imminent loss

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Note** officials will report further on options for clarifying EQC's settlement obligations regarding land damage

**Agree** that the EQC scheme not cover damage due to gradual deterioration associated with ongoing exposure to a covered peril, such as gases from hydrothermal vents or volcanism

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Agree** that damage from slow-moving landslips should *not* be considered a form of gradual deterioration

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Note** that some tsunami (meteotsunami) are caused by meteorological conditions rather than seismic activity

**Agree** that meteotsunami be considered a form of storm and flood in determining EQC cover applicable to these events

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

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**Agree** that EQC cover for damage caused by fires that are caused by a natural disaster be retained

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Note** that potential weaknesses in the current “natural disaster fire” definition will be raised with PCO at the drafting stage

**Connections to wider government risk management and response**

**Agree** that EQC should participate in broader whole-of-Government recovery plans and processes

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Agree** to refer to the Ministry for the Environment for consideration the suggestion that Resource Management Act 1991 (RMA) reforms should be made to enable EQC to legally carry out emergency works without a resource consent.

*Agree/disagree.*  
Minister Responsible for the Earthquake  
Commission

*Agree/disagree.*  
Associate Minister of Finance

**Opportunities for technical refinement in the new legislation**

**Note** that a range of other technical points and suggestions were made at the workshop that officials will pass onto PCO for consideration at the drafting stage.

Anna Everton  
**Acting Manager/Team Leader**  
**Financial Markets**

Hon Gerry Brownlee  
**Minister Responsible for the**  
**Earthquake Commission**

Hon Dr Jonathan Coleman  
**Associate Minister of Finance**



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EQC Act Review: Issues Identified at Natural Hazards Experts' Workshop

Loss of EQC Cover Following or in Anticipation of a Natural Disaster

Issue	Discussion and Analysis	Recommended Action
<p><b>Land cover linked to residential building cover is lost when the insured building is destroyed.</b></p> <p>For example, where a building is a constructive loss and fire insurance is cancelled following an earthquake and before the building is replaced, the land is damaged by another peril (e.g. flood).</p> <p>Floods are more likely following significant volcanism as the ash clogs waterways.</p>	<p>The loss of land cover when the insured building is destroyed reflects the broad objective of the EQC scheme – to provide first-loss cover on dwellings and the land on which they stand. However, in the event of sequential losses of building and land, there may well be public expectations of EQC compensation for the land loss.</p> <p>However extending EQC cover to bare land that previously was covered by EQC raises a range of difficult issues:</p> <ol style="list-style-type: none"><li>1. Precedent effects – it may be hard to not extend cover to all bare residential land.</li><li>2. Application of the 8 metre rule when the dwelling no longer exists.</li><li>3. It may be hard to time-limit any cover on bare residential land, diluting the scheme's focus on funding recovery.</li><li>4. Claims handling – the preferred reform package includes all claims being filed via claimants' private insurers, and in this case claimants no longer have private insurance policies.</li></ol> <p>In addition, increased vulnerability to hazards following a natural disaster is likely to provoke a wider policy response, as we are seeing with flooding in Christchurch.</p> <p>In some scenarios, dwelling owners would be compensated for land losses following the loss of the building under the "proximate cause" principle of insurance law if the land loss was a direct and inevitable consequence of the event that caused the loss of the building.</p>	<p><b>Note</b> that payout of a total loss insurance claim on a building leaves the associated land without EQC land cover until fire insurance is issued on a residential building rebuilt on the site.</p> <p><b>Confirm</b> that land cover continue to only be available to residential buildings with a qualifying fire insurance policy in place.</p>
<p><b>Loss of private insurance cover in times of volcanic unrest.</b></p> <p>Ongoing volcanic 'unrest' could lead to private insurers cancelling fire insurance cover for an area and so leave that area with no EQC cover.</p> <p>Such unrest could also lead to s124 notices under the Building Act 2004.</p>	<p>The widespread cancellation of private insurance cover raises two risks:</p> <ul style="list-style-type: none"><li>• EQC being swamped by many, potentially thousands, of s.22 requests for voluntary direct purchase of EQC cover;</li><li>• Political economy pressures to increase EQC coverage caps if private top-up cover is not available.</li></ul> <p>The first issue can be managed using the direct purchase provisions (s.22) of the existing Act. The second issue can be managed by in part by increasing the cap as part of the Review. Any increase in cap (and EQC premium) subsequent to insurers departing a geographical area reflecting the particular characteristics and scale of that event.</p> <p>In the event of a significant volcanic exclusion zone being imposed, future governments are likely to consider responses outside the scope of the EQC scheme, such as a residential red zone offer akin to that made in Canterbury.</p> <p>As the scheme covers "physical damage," building unavailability due to a s.124 notice being imposed is not currently an insurable loss (this was recently confirmed by the High Court in <i>Kraal &amp; Irvine v The Earthquake Commission &amp; Allianz New Zealand Limited</i>).</p>	<p><b>Note</b> that ongoing volcanic unrest could lead to private insurers cancelling fire insurance cover for an area, leaving that area with no EQC cover.</p> <p><b>Agree</b> to retain homeowners' existing ability under the EQC Act to buy EQC cover directly from EQC.</p> <p><b>Note</b> that ongoing volcanic unrest could result in notices being issued under s.124 of the Building Act preventing homeowners from entering badly affected properties.</p>

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EQC Scheme Coverage and Repair Powers

Issue	Discussion and Analysis	Recommended Action
<b>EQC should have powers to undertake area-wide land repairs</b>	<p>Officials agree that EQC's powers in this area should be enhanced.</p> <p>Appropriate scope of and constraints on the use of such powers will be informed by current EQC work on area-wide solutions in Canterbury. Area-wide repairs should be a more readily available option where such repair is the most cost-effective and otherwise appropriate way of dealing with the damage.</p> <p>These new powers will likely infringe existing property rights by giving enhanced powers of access to conduct repairs (including to properties not insured by EQC, or not currently damaged).</p>	<b>Agree</b> that the Bill include provisions to facilitate area-wide land repairs, where that is the most economical solution to meet EQC's repair obligations.
<p><b>Definition of "damage"</b></p> <p>The definition of "damage" should reflect concepts of sustained or permanent impact. This would make it clear that temporary impacts are not covered (e.g. salt water contamination of soils after a tsunami).</p> <p>Further work is needed on whether and how best to address 'increased vulnerability' to potential (future) damage that is not imminent and, whatever the approach, the Act must be very clear what EQC's obligations and options are regarding settlement.</p>	<p>There are three different ideas at play here:</p> <p><b>That EQC should only cover damage that is sustained or permanent.</b> This issue arose in discussions regarding salt contamination from tsunami. Although harmful it is also relatively short-lived as in New Zealand's high rainfall environment the salt rinses out relatively quickly.</p> <p><b>There are differing views on whether a change in risk profile from an event should result in insurable losses</b> (e.g. increased flood, liquefaction or rock fall risks in Christchurch). Under normal insurance principles, the change in risk would not be claimable. From a policy perspective, affected homeowners have not suffered an immediate physical loss (although future risks have changed), so compensation does not advance resilience or recovery; it simply compensates for economic losses.</p> <p>Building future resilience in the face of increased risk is achieved by engineering and regulatory responses rather than by payments to affected homeowners. Arguments to compensate for these losses hinge on perceptions of fairness – and the related political economy argument that if the losses are not covered, the government will be pressured by affected homeowners to extend coverage to include them after a disaster, in which case it would be better to recognise this and charge up front for the risk. We see the political economy risks as manageable because the Government has other responses, such as engineering and regulatory options, to help address homeowner concerns regarding changes in risk profile.</p> <p>Therefore, given the proposed purposes of the scheme, which focuses on the provision of resources to restore basic adequate dwellings and improving community resilience, not compensation for loss, we recommend that changes in risk profile not be an insurable loss. EQC cover would still apply if there was the prospect of an imminent loss (i.e. a loss that will almost certainly arise within 12 months).</p>	<p><b>Agree</b> that the EQC scheme only cover damage that is sustained or permanent.</p> <p><b>Agree</b> that changes in risk profile be an insurable loss only if as a result there is the prospect of an imminent loss.</p> <p><b>Note</b> officials will report further on options for clarifying EQC's settlement obligations regarding land damage.</p>
<p><b>Gradual deterioration</b></p> <p>Gradual deterioration is likely to be associated with prolonged volcanic and/or hydrothermal activity (e.g. gas corrosion, acid rain) and may currently be covered by the Act.</p> <p>Consideration needs to be given as to whether EQC cover should reflect private insurer practice and clearly exclude gradual deterioration.</p>	<p>The workshop identified acid rain from persistent volcanic ashfall (over months or years) and hydrothermal gases in Rotorua as the most likely cause of claims for gradual damage. The historic 3 month deadline for EQC claims effectively excluded gradual damage as only damage within the last 3 months could be claimed. Recent and proposed changes to deadlines for reporting claims create the possibility of claims for gradual deterioration.</p> <p>It is normal insurance industry practice to exclude losses due to gradual deterioration, as this form of damage is best managed directly by the building owner and its inclusion creates significant moral hazard issues.</p> <p>The building code in principle reflects the gradual deterioration challenges of the environment the building is in (e.g. Rotorua, coastal areas).</p> <p>Also, one of the conditions applying to EQC cover is that insured persons must take all reasonable steps to mitigate damage. As gradual damage occurs over extended periods of time, it would be reasonable to expect mitigation action by insured persons:</p> <p>The current EQC position is that it covers gradual damage flowing directly from acute events, such as rotting carpets or sub-floor decay due to liquefaction. Officials recommend that this treatment continue. The proposed change would make it clear that gradual damage associated with exposure</p>	<p><b>Agree</b> that the EQC scheme not cover damage due to gradual deterioration associated with ongoing exposure to a covered peril, such as gases from hydrothermal vents or volcanism.</p> <p><b>Agree</b> that damage from slow-moving landslips should <i>not</i> be considered a form of gradual deterioration.</p>



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	<p>to an ongoing hazard, such as corrosive hydrothermal fumes, would not be covered.</p> <p>Officials consider that damage from slow-moving landslips should <i>not</i> be considered a form of gradual deterioration, and so should <u>still</u> be covered by EQC. This is because repairing such slips is usually expensive and often requires area-wide repairs on multiple properties that it is not reasonable to expect homeowners to undertake themselves.</p>	
<p><b>Calculating entitlements with a dollar cap on land payouts.</b></p> <p>The Act needs to be clear how the proposed new land cap will be implemented, particularly with regard to retaining walls (e.g. will settlement be based on the amount to reinstate/replace a damaged wall up to the level of the land cap or is it restricted to any lesser amount of the value of the land impacted?).</p>	<p>The current dollar cap on an EQC payout for damaged land is the market value of the residential land plus the indemnity value of any retaining walls, bridges or culverts. These rules are a source of confusion for claimants and can generate inequitable results, with different claimants receiving markedly different levels of compensation for similar damage. The rules also need revision to reflect the introduction of a dollar cap on land payouts and the shift to full replacement value of retaining walls, bridges and culverts.</p> <p>The future reporting on options for clarifying EQC's settlement options for land damage will also provide advice on this issue.</p>	<p><b>None</b> (this issue will be picked up as part of the recommendation to direct officials to report further on options for clarifying EQC's settlement obligations regarding land damage).</p>
<p><b>Weather-initiated tsunami (meteotsunami)</b></p> <p>Some tsunami are have meteorological rather than seismic origins.</p> <p>Meteorologists consider meteotsunami to be a type of storm surge. Given their name, under current EQC legislation it is unclear whether they would be considered a tsunami (with EQC covering both land and building damage) or a storm (with EQC covering only land damage).</p>	<p>Given the categorisation of meteotsunami as a type of storm surge, the best fit with the existing EQC scheme would be to treat damage from these events as storm and flood damage.</p> <p>Defining storms to include meteotsunami would also be a more robust and administratively simpler boundary than defining tsunami to include meteotsunami. That is because meteotsunami and storms often occur together. If meteotsunami were treated as tsunami and a meteotsunami occurred, EQC would need to determine what damage was caused by tsunami (and hence triggering building as well as land cover) and what damage was caused by the rest of the storm (in which case only land cover applies).</p>	<p><b>Note</b> that some tsunami (meteotsunami) are caused by meteorological conditions rather than seismic activity.</p> <p><b>Agree</b> that meteotsunami be considered a form of storm and flood in determining EQC cover applicable to these events.</p>

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<p>The intention of the Act and <b>the need for EQC to cover ‘natural disaster fire’ should be reassessed</b> with particular consideration of how EQC cover interacts with private insurance cover for fire.</p>	<p>The EQC scheme currently covers “natural disaster fire”, that is fires caused by a covered peril. A participant suggested that this cover could be removed as private insurers already provide fire insurance.</p> <p>However removing explicit reference to “natural disaster fire” would do little to reduce the EQC exposure as under the “proximate cause” principle of insurance law, any fire that directly and inevitably resulted from an event, say an earthquake, would be treated for insurance purposes as if the event itself had directly caused the loss.</p> <p>Therefore “natural disaster fire” is probably a largely redundant provision. Given its removal would have little practical effect while also generating uncertainty, we recommend retaining the current provision.</p> <p>However investigating this issue did draw our attention to an apparent anomaly in the current Act. Although the policy intention is that the EQC scheme does not cover buildings against storm and flood damage, the current drafting appears to extend EQC cover to a building damaged by fire caused by land damage caused by a storm or flood. This is an unlikely chain of events and EQC is not aware of any claims having ever been made on this basis. We will raise this with PCO as a technical correction.</p>	<p><b>Agree</b> that EQC cover for damage caused by fires that are caused by a natural disaster be retained.</p> <p><b>Note</b> that potential weaknesses in the current “natural disaster fire” definition will be raised with PCO at the drafting stage.</p>
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Connections to wider government risk management and response

Issue	Discussion and Analysis	Recommended Action
<p><b>EQC’s role in whole-of-government recovery processes</b> needs to be considered alongside other recovery legislation and broader recovery issues.</p>	<p>Officials consider that there is value in EQC participating in broader whole-of-Government recovery plans and processes.</p> <p>The currently legislated functions of the Commission do not envisage this. If you agree to the recommendation we will include appropriate drafting instructions so PCO can consider whether any legislative change is desirable.</p>	<p><b>Agree</b> that EQC should participate in broader whole-of-Government recovery plans and processes.</p>
<p><b>Resource Management Act 1991 (RMA) reforms should be made to enable EQC to legally carry out emergency works without a resource consent.</b></p>	<p>Section 330 of the RMA confers powers on certain organisations (owners or operators of public works, network and lifeline utility operators, and local authorities) to carry out emergency works without a resource consent. These works typically relate to land works. The proposal is to add EQC to that list.</p> <p>We see this proposal as having complex implications. Simply adding EQC to the current list would give EQC a special status as the only organisation other than local government authorised to undertake works to protect other people’s property. This would be a unique role within central government. Such a role would pose significant strategic questions regarding EQCs role and purpose within the machinery of government (insurer or emergency responder). In addition, EQC would have powers that property owners themselves or other insurers (including of commercial and rural property) do not have.</p> <p>Therefore we consider that EQC should not be given any special status under the RMA to conduct emergency works. However we propose to refer this issue to the Ministry for the Environment (the administering department for the Resource Management Act) for consideration as to whether a less targeted extension of the current list of authorised emergency repairers is desirable.</p>	<p><b>Agree</b> to refer this suggestion to the Ministry for the Environment for consideration.</p>
<p><b>EQC should be more active/influential in land use planning processes.</b></p>	<p>The draft purpose clause for the EQC Bill includes the following wording: “support improving the resilience of New Zealand communities and therefore an efficient approach to the overall management of natural disaster risk and recovery in New Zealand.” This wording would provide sufficient basis for EQC to participate in land use planning processes if it wished to do so.</p>	<p><b>None.</b></p>

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<p><b>Consideration could be given to enabling EQC to signal in advance that it will not cover new residential developments it considers a poor risk</b> (i.e. at present EQC can only remove cover for dwellings where a full cap payment has already been made).</p>	<p>This proposal stemmed from some participants' concerns regarding the quality of natural hazard risk assessment in some planning approvals.</p> <div></div> <p>Therefore we recommend not pursuing this suggestion further.</p>	<p><b>None.</b></p>
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**Opportunities for technical refinement in the new legislation**

Issue	Discussion and Analysis	Recommended Action
<p>A range of other technical points and suggestions were made that officials will pass onto PCO.</p>	<p>These suggestions include:</p> <ul style="list-style-type: none"><li>• The Act should include definitions of flood and storm to distinguish more clearly between flood, debris flow, natural landslip and a storm (as EQC cover differs according to the peril).</li><li>• The Act should include a definition of "event". As EQC cover reinstates after each "event" it is crucial to clearly define what constitutes an event. (We intend reflecting current practice that all damage occurring within a 48 hour period (including from multiple perils) will be deemed to be a single event for the purpose of EQC insurance cover).</li><li>• The drafting should reflect the modern emphasis on building resilience to avoid disasters rather than an implied acceptance that disasters are inevitable. The suggestion is that the Act should use the term 'natural perils' rather than 'natural disasters'.</li><li>• The term volcanic 'eruption' is too narrow. The Act should refer to volcanic 'activity' given that there is a significant possibility of other 'unrest' and secondary hazards which are not strictly an 'eruption'.</li><li>• Inclusion of a purpose statement in the Act was strongly supported. The purpose statement could help clarify the relationship between building and land cover in the context of the Crown's housing-related interests.</li></ul>	<p><b>Note</b> that a range of other technical points and suggestions were made at the workshop that officials will pass onto PCO for consideration at the drafting stage.</p>