

The Treasury

Earthquake Commission (EQC) Act Review Submissions Information Release

Release Document

January 2018

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.



8 September 2015

Review of EQC Act
The Treasury
PO Box 3724
Wellington 6140
NEW ZEALAND

By email: submissions.eqcreview@treasury.govt.nz

EQC Act Review

Please find attached Southern Response's submission in respect of the proposed EQC Act Review. Not being a participant going forward but having been an active participant during the Canterbury recovery and indeed, having financially failed in its former guise as AMI, my Board believes that the company has an unique contribution to make.

All commentary is through Southern Response's lens, principally from its own experiences.

The key items we wish to highlight to the Review are:

The proposals and questions

- That a principal aim of the act should be to ensure that housing is available after a natural disaster.

This is intended to provide emphasis that there is a statutory framework that together with cash settlements, ably supports repairing and replacing damaged residential buildings following a natural disaster.
- Further that affordability and wide participation in the scheme to ensure comprehensive coverage for New Zealand's home owners should also be emphasised as a principle (purpose). The review seems to have ignored affordability and availability, particularly with the lift of the EQC cap to only \$200,000, well below the average price of a house in NZ, which is where the original cap was struck in 1993 and appeared to be the threshold for private insurance to kick in. Such a low level provides the potential for private insurers to risk rate for earthquake cover affecting the cost of such coverage above \$200,000 although it is acknowledged that, as we understand, there is no move in that direction.

Additionally, while agreeing that "site works" should replace land cover in the majority of circumstances, it is proposed that such site works be recognised as to their likely value, thereby further justifying the lifting the EQC cap. That is, the current system has two caps (land and building). The site works component (equivalent to land) should be similarly treated.
- That there should be prescription as to the respective responsibilities of the various parties in the recovery. For example, if cash becomes the remedy pursued by all agencies, including EQC, how would area-wide geotechnical investigation occur to the benefit of homeowners?
- That EQC cover should last until 12 months after the first event, provided the policy is renewed during that time. At the end of the 12 months the EQC cover reinstates for a broken period up to the next insurance renewal date. This will avoid the complexities of trying to assess and apportion damage where there are a series of events. Of course, reinsurance terms would need

- to be similarly structured and it is recognised that if implemented would reflect a bespoke arrangement, unique to New Zealand.
- That the new legislation should be structured with the aim of encouraging EQC and the insurance industry to work together with goodwill and cooperation and the free exchange of information.
- That the EQ excess should be much higher than \$2,000 as proposed to eliminate cosmetic claims from the core recovery focus.
- That we recognise the weakness in the current system regarding late advice by EQC of overcap claims and that any changes to legislation should seek to optimise available resource from EQC and the private insurance industry.
- In seeking to optimise resource, any move to shift the 'first response' to private insurers would benefit from regular independent assessments that private insurers have the systems, financial and other resources ready to scale up, be the notifying media for earthquake claims and to endure through the recovery. This independent assessment regime should be in place either prior to enactment or as an ongoing readiness assessment. We believe we would have benefitted from such a regime, particularly if we (rather than EQC) had been designated with part of the first response in the Canterbury earthquake sequence.

Operational considerations - Assessment and investigations

We have also considered regulatory issues that should be addressed dealing with some operational considerations. If the house is a repair in the current environment, the structural engineer takes the lead and the geotechnical investigations follow. For example, the structural engineer advises that the piles need jacking and packing, geotechnical investigations then follow to ascertain the shallow bearing capacity of the ground. If the house is to be rebuilt, the geotechnical engineer assesses the land conditions and makes recommendations as to the foundations that are appropriate.

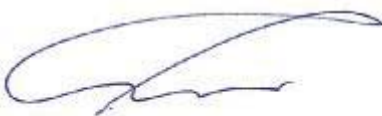
- Following the Canterbury earthquakes the EQC geotechnical engineers Tonkin & Taylor carried out widespread investigation of the land damage. Insurers carried out their own geotechnical investigations, as did some homeowners. There was similar duplication of structural engineering, particularly as between the insurer and the homeowner. This just wastes resources, costs and time. Regulations covering who is responsible for these assessments would reduce the duplication of investigations and the waste of resources.
- Assessments and investigations should form part of the claim handling and processing costs and should sit outside the EQC cap. If the insurer incurs these costs then provision should be made for the insurer to be reimbursed.

Other: Perils and hazards:

- Perils covered by EQC are mainly single event hazards or imminent threat. While coverage for "landslip" would include cliff collapse, rock roll threat would not be covered. We consider that New Zealand also faces longer timescale hazards e.g. sea level rise, coastal erosion. Some consideration should be given to how New Zealand, as a country, deals with these hazards.

Our submission in template form is **attached**.

Yours faithfully



Peter Rose
Chief Executive
Southern Response Earthquake Services Ltd



New Zealand's Future Natural Disaster Insurance Scheme

Proposed changes to the Earthquake
Commission Act 1993

Submission Form

July 2015

New Zealand's Future Natural Disaster Insurance Scheme Proposed changes to the Earthquake Commission Act 1993

Your responses

Please write your response in the template below.

Please note:

- ▶ you **do not** need to answer all sections – just the ones where you have information you would like to contribute
- ▶ please expand or delete boxes as you need to but **do** keep the original question numbers.
- ▶ please **do not** send us reports or other documents but **do** include references or links to supporting evidence or information
- ▶ please submit your response to Submissions.Eqcreview@treasury.govt.nz by 5.00pm on Friday 11 September 2015.

Thank you for your time and effort in making your submission.

Official Information Act 1982

Submissions are subject to the Official Information Act 1982 (OIA). Please set out clearly with your submission if you have any objection to any information in the submission being released under the OIA, and in particular, which part(s) you consider should be withheld, together with the reason(s) for withholding the information.

Grounds for withholding information are outlined in the OIA. Reasons could include that the information is commercially sensitive or that you wish personal information, such as names or contact details, to be withheld. An automatic confidentiality disclaimer from your IT system will not be considered as grounds for withholding information.

We will take your objections into account when responding to requests under the OIA.

Any personal information you supply in the course of making a submission will be used by the Treasury only in conjunction with the matters covered by this document. Please clearly indicate in your submission if you do not wish your name to be included in any summary of submissions that we may publish.

Your contact details

For individuals

Your name:	
	Indicate here if you do not wish your name to be included in any summary of submissions that we may publish.

Email address:	
Phone number:	

What city, town or province do you live in?	
Do you own your own home?	

For organisations

Organisation name:	Southern Response Earthquake Services Limited
Nature of your business:	Earthquake claims management company

Contact person name:	Peter Rose
Position:	Chief Executive
Phone number:	[1]
Email address:	

In what city, town or province is your organisation's New Zealand headquarters?	Christchurch
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Appendix 1: Proposals and questions for submitters

What is the purpose of the EQC scheme?

Proposal for discussion

1 That the purpose of the EQC Act be to establish a Crown-owned natural disaster insurance scheme for residential buildings in New Zealand that: supports, complements and is closely coordinated with the provision of effective private insurance services to the owners of residential buildings recognises the importance of housing in supporting the recovery of communities after a natural disaster

- supports improved resilience of New Zealand communities and an efficient approach to the overall management of natural hazard risk and recovery in New Zealand contributes to the effective management by the Crown of fiscal risks associated with natural disasters.

What do you think?

1a Do you agree that these purposes are appropriate and complete?

Appropriate **Yes but not complete.**

1b If not, what changes would you suggest, and why?

The principal aim should be to ensure that the affected members of the community are able to be back into their homes as quickly as possible after a natural disaster. So purposes 2 and 3 above should be the leading purposes. A further purpose should be included:

affordability and wide participation in the scheme to ensure comprehensive coverage for New Zealand's home owners.

The statutory regime should also continue to ensure that together with any cash settlement that an affected owner may choose, there is a programme of works of sufficient scale and accessibility to those individuals with damaged homes that need professional support to have their home repaired or rebuilt. This will ensure that recovery objectives are supported. See also sections 17b and 23.

What types of perils will EQC cover?

Proposal for discussion

2 That EQC continue to insure against the following perils: earthquake, natural landslip, volcanic eruption, hydrothermal activity, tsunamis, and storm and flood (with, in the case of storm and flood, only residential land being covered).

What do you think?

2a Do you agree that EQC should continue to provide cover against the same perils as it currently does?

Yes but see further comment below in 2b.

2b If not, what changes would you suggest, and why?

*We assume that "landslip" includes cliff collapse. Rock roll threat is not covered
Most of the perils covered by EQC relate to single event perils or imminent threat.
Coastal erosion could be considered along with sea level rise.[see covering letter]*

What types of property will EQC insure?

Proposal for discussion

3 That EQC building cover continue to be available to residential buildings and dwellings in non-residential buildings.

What do you think?

3a Do you agree that EQC building cover should continue to only be available to residential buildings and dwellings in non-residential buildings?

Yes, but see comments in 3b.

3b If not, what forms of accommodation or living arrangements do you think should be added or removed, and why?

The principles under which cover applies are inconsistent. Retirement villages where the units are owned by the residents are covered but units occupied under a licence are not. Retirement villages are generally commercial operations. Should a distinction be made between owner occupied units or licenced units or serviced apartments occupied by the elderly if the aim of the legislation is to ensure housing is available after a natural disaster to all residents including the vulnerable?

Proposal for discussion

4 That EQC land cover only be available for land associated with residential buildings. Therefore, dwellings in non-residential buildings would not receive any EQC land cover.

What do you think?

4a Do you agree that EQC land cover should only be available for land associated with residential buildings?
Yes

4b If not, what coverage of land cover would you prefer, and why?

Extending building cover to include more siteworks and main access way

Proposal for discussion

5 That EQC building cover be extended to include section 5 works and the main access to the building.

What do you think?

5a Do you agree that EQC building cover be extended to include siteworks and the main access to the building?
Yes but see comments in 5b

5b If not, what do you think should be done instead, and why?

1. Siteworks is described in the paper as including the geotechnical investigations, land works, access ways and retaining walls needed to support or protect the building. We agree with this but consider it needs more clarity.
2. Siteworks can be extensive and expensive particularly where ground remediation or significant foundation work is required. This will quickly erode the value of the building cap and this is one reason why we suggest that the cap should be increased to ensure that the majority of the housing stock can be addressed by the statutory regime (see 7b).
3. There is a conflict between the roles of the geotechnical and structural engineers. A practical process about who makes decision is needed. If the claim is going to the insurer first, who is best placed to do the engineering and make the decisions? One party should be responsible for all assessment and engineering.
4. Assessment including geotechnical and structural engineering investigations are part of the investigation and claims processing. This should be considered part of claims handling and administration and should not be included in the cap. Some regulations and protocols will need to set up to ensure that the costs of this claims handling and administration are reimbursed to the insurer separately from the cap.
5. Some commentators suggest a separate cap for siteworks. We have considered this but believe that the distinction between the building platform and the building is too blurred to be differentiated in significant numbers of cases.

EQC to no longer provide contents insurance

Proposal for discussion

6 That EQC no longer offer residential contents insurance.

What do you think?

6a Do you agree that EQC should no longer offer residential contents insurance?

Yes

6b If not, what level of contents cover do you think EQC should offer, and why?

6c For insurers, what do you anticipate the impact would be on premiums your company charges for residential contents insurance, if EQC no longer offered residential contents insurance? Please note the information in section 1.4 regarding the Official Information Act.

How much insurance will EQC offer?

Proposal for discussion

7 That the monetary cap on EQC building cover be increased to \$200,000 + GST.

What do you think?

7a Do you agree with the proposed increase in the building cap to \$200,000 + GST?

No

7b If not, what cap would you prefer, and why?

The cap of \$100,000 +GST was originally set at the cost to build an average 100m² home at that time. This was for very practical purposes: to ensure that EQ cover would be affordable (flat rating) regardless of risk location, and to ensure the average home could be replaced under the EQC scheme. This value has been eroded over time.

We consider there are strong social grounds on which to reinstate a similar formula for the cap: it should be a figure sufficient to cover the costs of rebuilding a house to cover the 80th percentile of residential homes. .

Additionally, the “standard” cost of site works (replacing land cover – section 5b) justifies a higher cap (given that building and land damage now have separate caps).

If the cap is a low figure and insurers have got sufficient risk they will price it accordingly. A higher cap will provide protection against insurers risk rating.

7c Do you have strong views on the merits of a \$150,000 + GST cap versus a \$200,000 + GST cap?

Yes

7d If so, what are they?

\$200,000 + GST is too low and does not still appear to meet one of its original purposes – see comments in 7b.

7e For insurers, what do you anticipate the impact would be on premiums your company charges for residential property insurance, if the proposals in this document regarding changes to building cover were implemented? Please provide this information for a monetary cap for EQC building cover of both \$150,000 and \$200,000.

Please note the information in section 1.4 regarding the Official Information Act.

Reinstatement of EQC cover after an event

Proposal for discussion

8 That EQC building cover reinstate after each event.

What do you think?

8a Do you agree that EQC cover should reinstate after each event? If not, what is your preferred alternative, and why?

No. The EQC cover should last until 12 months after the first event provided the policy is renewed during that time. At the end of the 12 months the EQC cover reinstates. This will avoid the complexities of trying to assess and apportion damage where there are a series of events in most circumstances. It is noted that reinsurers' corresponding cover would need to be especially negotiated. The only issue would be if the house is repaired after one event but before the next event during the 12 month period.

It is recognised that if implemented, it would reflect a bespoke reinsurance arrangement, unique to New Zealand

8b Do you agree with retaining the current definition of an event?

Yes

8c If not, what is your preferred definition, and why?

EQC land cover

Proposal for discussion

9 That land cover be limited to situations where the insured land is a total loss meaning it is not practicable or cost-effective to rebuild on it.

What do you think?

9a Do you agree that the proposed enhanced building cover, combined with restricting land cover to situations where the site of the insured building cannot be rebuilt on, would resolve, for future events, many of the recent difficulties with the interaction between land and building cover?

Yes But see 5 above in relation to investigation work

9b If not, what is your preferred alternative, and why?

9c Do you agree that restricting land cover to situations where the site of the insured building cannot be rebuilt on is appropriate, given the EQC scheme's focus on providing homeowners the resources to repair, rebuild or re-establish homes elsewhere? Yes.

However who determines it is not practicable or cost-effective to rebuild on this land? Note that in Canterbury the red zoning of land was done under the CERA legislation not the EQC Act.

9d If not, what is your preferred alternative, and why?

9e Do you have any concerns regarding the proposed change to the configuration of building cover in light of the move by most insurers to provide sum insured home insurance policies? Only that the EQC cap should be higher to cover off the site works.

9f If so, what is your preferred alternative, and why?

Better aligning EQC and private insurers' standard of repair

Proposal for discussion

10 That EQC's current statutory repair obligation already appears broadly consistent with industry practice.

What do you think?

10a Do you agree with the Government's assessment that EQC's legislated standard of repair is broadly consistent with current industry norms?

Yes however insurance norms vary (which can be to different standards).

10b If so, do you have views on why EQC's standard of repair is seen as markedly different from current insurance industry norms?

This is mainly operational differences. For example EQC has taken the view that although there is EQ damage it does not have to relevel the house because the MBIE guidance does not require it be relevelled if <50mm out of level. Repair "to the standards of the Building Act" should prevail.

10c If not, do you have suggestions for reforms that you consider would move the EQC standard of repair closer to current insurance industry norms for residential property?

We suggest something along the lines of the VERO definition set out on pg 30 is suitable.

Also the repair standard can be defined to include "to Building Code standards". Note the current EQC Act requires compliance with "any applicable laws"

Simplifying EQC's claims excess

Proposal for discussion

11 That EQC has a standard claims excess of \$2,000 + GST per building claim.

What do you think?

11a Do you agree that EQC's building claims excesses should be standardised and simplified to a flat dollar amount?

Yes

11b If yes, do you agree that \$2,000 + GST is the appropriate claims excess on building claims? No

11c If not, what would you prefer, and why?

\$2000 + GST is too low. We suggest \$5000 + GST. This would discourage very minor claims. The excess should be set at a level that the coverage is triggered when a repair is required not redecoration. In that manner, the recovery would be more orderly: priorities addressed.

Our actuary's review of the EQC data for our undercap claims indicates that more than 50% of our undercap claims were under \$15,000 and the average value was just over \$6000.

Proposal for discussion

12 That EQC have no claims excess on land claims.

What do you think?

12a Do you agree that EQC should have no claims excess on land claims?

Yes

12b If not, what would you prefer, and why?

Regularly reviewing main monetary settings of cover

Proposal for discussion

13 That the EQC Act require monetary caps, premium rates and claims excesses on EQC cover to be reviewed at least once every five years.

What do you think?

13a Do you agree that monetary caps, premium rates and claims excesses on EQC cover should be reviewed at least once every five years?

Yes and that a framework for that consideration be provided

13b If not, what alternative would you prefer, and why?

How will homeowners access EQC insurance cover?

Proposal for discussion

14 That EQC cover continues to automatically attach to fire insurance policies on residential buildings, as defined in the EQC Act. or

15 That EQC cover automatically attach to insurance policies on residential buildings, as defined in the EQC Act, on a peril by peril basis; so if a peril covered by EQC is excluded from the private policy, it is also excluded from the EQC cover.

What do you think?

14a Do you agree that EQC cover should continue to automatically attach to fire insurance policies on residential buildings? Or Yes

[Note that "fire only" insurance policies are rare these days; nowadays the policies are known as "general" house policies]

15a do you agree that EQC cover should automatically attach to insurance policies on residential buildings, and EQC cover should exclude any natural disaster peril that is excluded from the fire insurance policy it attaches to?

Yes

15b If you do not agree with either of these options, what alternative arrangement do you prefer, and why?

Proposal for discussion

16 That EQC continue to have the ability, but not the obligation, to directly provide EQC cover to homeowners who request it.

What do you think?

16a Do you agree that EQC should continue to be able, but not be obliged, to directly provide EQC cover to homeowners who request it?

Yes

16b If not, what alternative arrangement would you prefer, and why?

Who will handle EQC claims in future?

Proposal for discussion

17 That all EQC claims be lodged with claimants' private insurers.

What do you think?

17a Do you agree that EQC claimants should be required to lodge all EQC claims with claimants' private insurers?

Yes but see 17b.

17b If not, what alternative arrangement would you prefer, and why?

This query appears to have two dimensions: the notification agency and the ongoing management of the claim.

We recognise the weakness in the current system regarding late advice by EQC of overcap claims and that any changes to legislation should seek to optimise available resource from EQC and the private insurance industry.

In seeking to optimise resource, any move to shift the 'first response' to private insurers would benefit from regular independent assessments that private insurers have the systems and resources ready to scale up and be the notifying media for earthquake claims. This independent assessment regime should be in place either prior to enactment or as an ongoing readiness assessment. We believe we would have benefitted from such a regime, particularly if we (rather than EQC) were designated with first response in the Canterbury earthquake sequence.

Alternatively, the EQC, itself, scheme if it was the chosen 'first response' mechanism, would also benefit from ongoing regular independent review. Given it only responds to natural disasters, careful consideration would need to be given as to how it transitions and scales to responding to a natural disaster (as compared with a larger workforce in the insurance industry). It is recognised that EQC remains a way that the Government can manage the residential recovery if it wishes to, or outsource it to private insurers.

Keeping the claim and initial assessment with EQC although potentially not providing immediate scale, does allow Government to consider its desired approach to managing a recovery following a natural disaster.

Deadline for reporting claims

Proposal for discussion

18 That the current three-month time limit for claims notification be retained, but EQC be able to accept claims up to two years after an event, unless doing so would prejudice EQC.

What do you think?

18a Do you agree that the current three-month time limit for claims notification should be retained, but EQC should be able to accept claims up to two years after an event, unless doing so would prejudice EQC?

Yes, if the discretion is fairly exercised.

18b If not, what alternative arrangements would you prefer, and why?

Ensuring the scheme meets its expected costs

Proposal for discussion

19 That the new EQC Act contain pricing and transparency principles requiring the scheme to adequately compensate the Crown for its expected costs and risks.

What do you think?

19a Do you agree that the new EQC Act should contain pricing and transparency principles requiring the scheme to adequately compensate the Crown for its expected costs and risks? Yes

19b If not, what alternative arrangements would you prefer, to ensure the scheme's future financial sustainability, and why?

Allow but do not require differentiated EQC premiums

Proposal for discussion

20 That the current legislative flexibility to charge flat-rate or differentiated EQC premiums be retained.

What do you think?

20a Do you agree that the current flexibility to charge flat-rate or differentiated EQC premiums should be retained?

Yes

20b If not, what alternative arrangement would you prefer, and why?

20c Do you agree with the Government's intention to continue charging EQC premiums at a universal flat rate?

How will EQC finance its risk?

Proposal for discussion

21 That the Natural Disaster Fund be retained in broadly its current legislative form.

What do you think?

21a Do you agree that the Natural Disaster Fund should be retained in broadly its current legislative form?

Yes

21b If not, what changes would you like to see considered?

Proposal for discussion

22 That the Act enable EQC to use other forms of risk transfer, in addition to traditional reinsurance.

What do you think?

22a Do you agree that the Act should enable EQC to use other forms of risk transfer, in addition to traditional reinsurance?

Yes

Do you have any other feedback?

Other feedback

23a Are there any issues not discussed in this document that you would like to bring to the Government's attention at this stage?

Exchange of information and cooperation

Assessment and administration costs

23b What submissions would you like to make on those issues?

The new legislation should be structured with the aim of encouraging EQC and the insurance industry to work together with goodwill and cooperation and the free exchange of information. The underlying reason would be to promote prompt and accurate assessments of damage, repair scope and costings and settlement of claims as fast as reasonably possible.

If insurers are managing the claims and carrying out the assessments (including what will be a large number of undercap claims) there should be a mechanism for the insurers to get compensated for those assessment and administration costs.