

The Treasury

Material Provided to the Public Inquiry into EQC Information Release

August 2021

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- [23] 9(2)(a) - to protect the privacy of natural persons, including deceased people
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- [31] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility
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- [36] 9(2)(h) - to maintain legal professional privilege
- [37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

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Date: 26 October 2011

To: Minister of Finance

Aide-Memoire: Meeting on the EQC Review

We are meeting you at 1pm on Tuesday 1 November to discuss options for the review of EQC's disaster insurance arrangements. We would like to seek your views on:

- The objectives sought from the review.
- Your preferences regarding the main choices for the review (scope, form, timing).
- Next steps, including when you would like to engage with your colleagues.

This aide-memoire outlines our initial thinking on the main choices available to you in scoping the review.

What are the Government's main interests in this area?

We see the Government's overall objective with regard to natural disasters as being to maximise national welfare over time, taking into account the full range of pre-disaster costs (mitigation, insurance, etc) and post-disaster costs (disruption, recovery, etc).

In the immediate context of a disaster, 'maximising national welfare' means minimising the distress of affected citizens, minimising wider disruption to New Zealand's society and economy, and supporting the recovery of the affected area. In ordinary times, it means reducing the potential for distress and disruption in *future* disasters by:

- Striking an economically and socially optimal balance between the acceptance, avoidance, mitigation and transfer of natural disaster risk.
- Prudently managing the fiscal risk associated with natural disasters.

Proposed objective

With this context in mind, we suggest the objective of the review be to **minimise the social cost associated with private property damage in natural disasters.**

Scope

We suggest the review focus on issues associated with disaster insurance arrangements rather than expand to cover the Government's overall approach to emergency response and disaster recovery. There are two reasons for this:

- The overall recovery framework is only one among many considerations influencing the degree to which the Government is willing to accept private sector risk.

- We do not want the review to become too broad and unwieldy.

Principles to guide the review

We also suggest the following principles to guide the development of the review:

- Individuals and communities are ultimately responsible for their own safety and for the security of their livelihoods. Policy should **support** – rather than replace – the actions of private parties in managing the risks they face.
- Policy should generate strong **incentives** for the optimal management of risk. In particular, policy should discourage moral hazard and encourage the avoidance, mitigation or transfer of risk where such options are economically beneficial.
- Policy should be **fair**. This does not necessarily mean that all citizens should be treated in exactly the same way, but rather that the basis for treating different groups of citizens should be transparent and justifiable.
- Policy must be **fiscally sustainable** over the long term.
- Policy should strike an appropriate balance between **flexibility** and **durability**.

The main choices

Taking the proposed objective as a starting point, we see three choices regarding the scope of the review:

| Choice | Preliminary Treasury thinking |
|--|--|
| How broad and wide-ranging will the review be? | A first principles review of how NZ manages the natural disaster risk associated with private property is desirable for two reasons: <ul style="list-style-type: none"> • The magnitude of the risks the Government faces. • The time elapsed since the last full scale review of the EQC scheme. |
| Who should lead the review? | The nature of the review team will depend to a large degree on the scope of the review, but a Treasury-led review drawing upon specialist external expertise is a feasible option. |
| How soon to make a start? | We suggest launching the review in July 2012 to allow time for: <ul style="list-style-type: none"> • EQC to reach a steady state in terms of its operational responsibilities. • Insurance markets to settle down. • The emotions raised by the quake to subside. Internal Treasury work to prepare for the review could commence early in the New Year. |

The attached A3 sets out these three main choices and some of their implications. We look forward to discussing these issues with you on Tuesday.

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OPTIONS FOR REVIEW OF EQC'S DISASTER INSURANCE ARRANGEMENTS

PURPOSE OF TODAY'S DISCUSSION

Ministers have publically committed to a 'full review' of the EQC.

With this in mind, we'd like to discuss:

- Potential objectives for the review.
- The main choices for the review and their implications.
- Next steps.

Context

- 1. The earthquake event has not yet finished.** This has 3 implications:
 - Govt is still operating in an environment of significant uncertainty.
 - Emotions continue to run high, especially because many insurance claims remain open and won't be settled anytime soon.
 - The insurance industry can't adjust to a 'new normal' until it knows where it stands – both in terms of seismic risk and potentially also Govt policy.
- 2. The insurance industry faces a major structural adjustment.**

We expect to see greater risk differentiation and product innovation in the future. But we don't know how soon and in what ways insurers will adjust.
- 3. There is significant public and industry interest in the review.**

Considerations regarding the review

- 1. Time-consistent policy is desirable.**

Rapid reversals in policy in the next few years will undermine public confidence in the Govt's approach to natural disaster management.

Bottom line: some degree of public/political consensus is needed to embed any change resulting from the review over the long term.
- 2. Government needs to keep an eye on the long term.**

Govt should be aware of the current situation in insurance markets, but not overweight short-term considerations if the intention is to establish policy enduring over decades.
- 3. The Crown's actions in Canterbury have created new public expectations.**

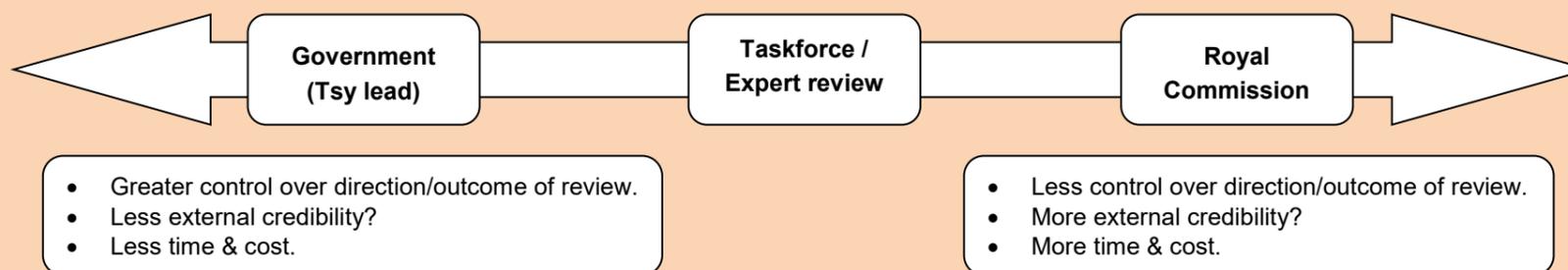
These expectations will influence and may constrain the Govt's options.

KEY CHOICES FOR MINISTERS

Scope: how broad and wide-ranging will the review be?

| Options | Advantages | Disadvantages |
|--|--|--|
| 1. First principles review of how NZ manages natural disaster risk associated with private property. <ul style="list-style-type: none"> • How should the Crown approach this risk? What is an appropriate set of objectives & principles? • What mechanisms are available to manage risk, aside from the EQC model? What are the costs & benefits of these options? | <ul style="list-style-type: none"> • Allows for complete survey of options available to Govt. • May identify major opportunities to improve management of disaster risk. | <ul style="list-style-type: none"> • Policy uncertainty for insurance markets until review concludes. • Time & resource intensive. • Risk of scope creep: review may drift into related but non-core issues, e.g. emergency management framework. |
| 2. Medium-scale review. <ul style="list-style-type: none"> • Can Govt make EQC model work better? • Issues may include extent & definition of cover; size & composition of NDF; interaction with private insurers. | <ul style="list-style-type: none"> • Clear opportunities to improve current system. • Greater certainty for insurance markets about end-state. | <ul style="list-style-type: none"> • May miss some opportunities to improve NZ management of disaster risk. |
| 3. Mini-review. <p>Operational tweaks & fixes.</p> | <ul style="list-style-type: none"> • Can be progressed quickly. • High certainty for insurance markets about end-state. | <ul style="list-style-type: none"> • Will miss major opportunity to improve NZ management of disaster risk. |

Who should lead the review?



The scope of the review will influence the choice about who leads the review, but these options can be mixed to some extent. For example, Treasury might lead the review, but task some pieces of work to a group of independent experts.

Timing: how soon to make a start?

