The Treasury

Material Provided to the Public Inquiry into EQC Information Release

August 2021

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Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

[23] 9(2)(a) - to protect the privacy of natural persons, including deceased people

[25] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information

[26] 9(2)(ba)(i) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely to prejudice the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied

[31] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility

[33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials

[34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;

[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

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [23] appearing where information has been withheld in a release document refers to section 9(2)(a).

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THE TREASURY
Kaitohutohu Kaupapa Rawa

Treasury Report: EQC: Direction to allow diversification of the Natural Disaster Fund

Date:	29 October 2001	**Treasury Priority:**	Medium
Security Level:	In-Confidence	**Report No:**	T2001/1766

Action Sought

	Action Sought	Deadline
Treasurer/Minister of Finance	Sign attached letter Lay copy of direction before House of Representatives Return copy of direction for gazetting	Tuesday, 30 October 2001 Thursday, 1 November 2001 Thursday, 1 November 2001
Associate Minister of Finance (Hon Trevor Mallard)	Note	None
Associate Minister of Finance (Hon Paul Swain)	Note	None

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
Tim Mitchell	Principal Advisor, Commercial Investments	[39]	[23]	✓
Gerry Verhaart	Senior Analyst, Commercial Investments	[39]	[23]	

Attachments: Letter to Earthquake Commission Chairman
Copy of direction to lay before House of Representatives
Copy of direction to return to Treasury to be published in Gazette

Treasury Report: EQC: Direction to allow diversification of the Natural Disaster Fund

On 3 October 2001 you wrote to the Chairman of the Earthquake Commission setting out the draft of a direction you intended to issue regarding the Natural Disaster Fund and seeking the Commission's comments on that draft (T2001/1647 refers). The Chairman has now responded. He suggested a number of minor changes to the draft to clarify the intent of the direction. EQC consulted with Treasury in making those changes and we agree that they represent improved drafting.

You have now fulfilled the consultative requirements set out in the EQC Act 1993 and may issue the direction to allow diversification to proceed. A letter to the Chairman of EQC is attached for that purpose.

The Act requires that as soon as practicable after issuing the direction, you lay a copy before the House of Representatives and publish a copy in the Gazette. Two copies of the direction are attached for those purposes.

EQC have suggested, and we concur, that a coordinated response to media enquiries would be preferable to ensure a consistent message regarding the benefits and risks of diversification is delivered. In the annex to this report we have included a series of questions and answers that may assist you or your office in dealing with media enquiries on this matter. After consultation with Treasury and EQC, your office has prepared a media statement that can be released on the day you lay a copy of the direction before the House of Representatives.

Recommended Action

We recommend that you:

a **note** the consultative requirements set out in the EQC Act 1993 have been fulfilled;

b **sign** the attached letter to the Chairman of the Earthquake Commission;

c **lay** a copy of the direction before the House of Representatives; and

d **return** a copy of the direction to officials for publishing in the Gazette.

Tim Mitchell
Principal Advisor, Commercial Investments
for Secretary to the Treasury

Hon Dr Michael Cullen
Minister of Finance

Questions and Answers: **Direction to Earthquake Commission**

Question: Why does EQC need to diversify?

Answer: It is prudent to hold assets outside the region that will be directly affected in the event of a major earthquake. If necessary, international equities can be liquidated quickly and, meanwhile, the investment will enhance returns over time.

Question: Why now?/Why not earlier?

Answer: Diversification has been under consideration for some time. The process, however, required detailed discussions involving EQC, Treasury and advisors before an agreement was reached about the best way to diversify the Natural Disaster Fund.

Question: How was the figure of 30% in international equities determined and why wasn't it some other number like 20% or 50%?

Answer: The 30% allocation is considered by EQC to be the proportion of international equities that best meets its claims payments requirements over time. The decision was guided by advice received from global investment advisory firm, Frank Russell.

Question: Why are there no NZ shares in the portfolio?

Answer: It is prudent to hold assets outside the region that will be directly affected. In the event of a natural disaster NZ equities may also suffer loss of value and may be difficult to sell quickly.

Question: Will there be an impact on the Government's debt programme?

Answer: No, provision has already been made in the Government's bond programme to provide the funding necessary for the diversification of EQC's investments

Question: Will there be an impact on the foreign exchange market?

Answer: Any impact will be minimal. The process of investing in equities is to be spread over two years.

Question: Who will manage the overseas shares?

Answer: Management of the international equities portfolio(s) will be outsourced. The best qualified international equities managers will be appointed to manage the portfolio(s).

Question: Will there be any impact on premiums?

Answer: No. Premium rates are set by legislation.

Question: In the event of an earthquake, what will be sold first – the shares or the bonds?

Answer: It will depend on the size of the earthquake, claims lodged, reinsurance policies in place, the state of the market and the economic environment at the time. Meanwhile, the diversified portfolio will provide the country with increased options for cash to meet claims payments.

Question: Is it a wise move to buy shares given current circumstances?

Answer: Current market circumstances don't affect the decision to begin the process now as the strategy is designed for the long-term. Investment in equities will be made progressively over a two-year period and returns will be measured over the long-term.

Mr Neville Young
Chairman
Earthquake Commission
PO Box 311
WELLINGTON

Dear Neville

DIVERSIFICATION OF THE NATURAL DISASTER FUND

Thank you for your letter of 16 October 2001. Pursuant to Section 12 of the Earthquake Commission Act 1993 I now issue a new direction regarding investment of the Natural Disaster Fund. The direction will take effect from 1 November 2001, on which day I intend to lay a copy of it before the House of Representatives.

Yours sincerely

Hon Dr Michael Cullen
Minister of Finance

Attachment: Direction to the Earthquake Commission pursuant to Section 12 of the Earthquake Commission Act 1993.

Direction to the Earthquake Commission pursuant to Section 12 of the Earthquake Commission Act 1993.

i. This direction comes into effect on 1 November 2001 and as of that date the direction dated 2 June 1998 is hereby revoked.

ii. The Earthquake Commission (the Commission) shall invest the Natural Disaster Fund (the Fund) in:

   (a) NZ Government securities comprising Treasury bills and/or Government stock and/or Inflation-Indexed Bonds tradeable only through the NZ Debt Management Office;

   (b) global equities; and

   (c) New Zealand bank bills.

iii. The Commission shall invest the Fund with the objectives of:

   (a) achieving an average rate of return of at least 1% per annum over the Crown's cost of borrowing over a rolling ten year period (where the Crown's cost of borrowing is measured by the change in the CSFB New Zealand Government Stock Gross Index);

   (b) subjecting the Fund to no more than 1 chance in 4 that over any 10 year period the annual rate of return will be less than the Crown's cost of borrowing; and

   (c) ensuring that there is no more than 1 chance in 30 of the Fund incurring an investment return of less than negative 2% in any one financial year.

iv. The Commission must invest the Fund on a prudent, commercial basis, and in doing so, must manage and administer the Fund in a manner consistent with:

   (a) best practice portfolio management;

   (b) maximising return without undue risk to the Fund as a whole; and

   (c) avoiding prejudice to New Zealand's reputation as a responsible member of the world community.

v. The Commission must prepare, and adhere to, a statement of investment policies, standards, and procedures for the Fund that is consistent with paragraph iv of this direction.

vi. The Commission must review those investment policies, standards, and procedures for the Fund at least annually.

vii. A statement of investment policies, standards, and procedures must cover (but is not limited to):

(a) the classes of investments in which the Fund is to be invested and the selection criteria for investments within those classes;

(b) the determination of benchmarks or standards against which the performance of the Fund as a whole, and classes of investments, will be assessed;

(c) standards for reporting the investment performance of the Fund;

(d) ethical investment for avoiding prejudice to New Zealand's reputation as a responsible member of the world community;

(e) the balance between risk and return in the overall Fund portfolio;

(f) the fund management structure;

(g) the use of options, futures, and other derivative financial instruments;

(h) the management of credit, liquidity, operational, currency, market, and other financial risks;

(i) the retention, exercise, or delegation of voting rights acquired through investments;

(j) the method of, and basis for, valuation of investments that are not regularly traded at a public exchange; and

(k) prohibited or restricted investments or any investment constraints or limits.

viii. The Commission must consult with the Minister of Finance (the Minister) if it intends to modify the statement of investment policies, standards, and procedures to any substantive degree.

ix. The Commission must consult with the Minister if it intends to modify the portfolio composition from the following:

(a) NZ Government securities;

(b) up to a maximum of 35% of the market value of the Fund in global equities; and

(c) up to a maximum of $250 million of New Zealand bank bills.

x. The Commission must consult the Minister if it forms the intention to cover its pre-disaster currency exposures and may not proceed with the implementation of a hedging strategy without the consent of the Minister being first had and obtained.

xi. In the event of a major natural disaster likely to involve claims on the Commission in excess of $250 million the Commission must consult with the Minister before liquidating any part of the investment portfolio of the Fund apart from the holdings of New Zealand bank bills.

xii. If the Commission considers at any time that any provision in this direction is inconsistent with another provision in this direction or any other direction under Section 12 of the Earthquake Commission Act 1993 or any provision under that Act it shall advise the Minister of that inconsistency.

Hon Dr Michael Cullen
Minister of Finance

30 October 2001