

The Treasury

Treasury Advice Related to Modernising the EQC Act Information Release

December 2021

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<https://www.treasury.govt.nz/publications/information-release/treasury-advice-related-modernising-eqc-act-information-release>

Clarifying Statement

In relation to page 14, section 2.4, paragraph 2:

For clarification: Consultation on a potential time bar related to EQC claims only.

Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

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:

- [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
- [27] 9(2)(ba)(ii) - 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 otherwise to damage the public interest
- [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
- [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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Regulatory Impact Statement: EQC Act Technical Issues

Summary: Problem and Proposed Approach

Problem Definition

The EQC Act's effectiveness was tested by the Canterbury earthquake sequence

The Earthquake Commission (EQC) provides natural disaster insurance cover for damage to privately insured residential properties. EQC plays a critical role in New Zealand's ability to recover from natural disaster events. Recovery from natural disaster events supports New Zealand's living standards across health, housing, safety and security, and subjective wellbeing domains.¹

During 2010 and 2011, the Canterbury region experienced New Zealand's most significant earthquake sequence in modern times. The EQC scheme's effectiveness was severely tested by the earthquake sequence in Canterbury:

- there was a lack of transparency around and clarity of the roles and responsibilities of EQC
- EQC's claims handling system was significantly overburdened, leading to negative experiences for claimants.² This was exacerbated by a lack of understanding of, and mismatched expectations around, the claims handling and settlement process
- a lack of clarity and certainty around entitlements under the Earthquake Commission Act 1993 (EQC Act) including the scope of cover for both land and buildings
- boundary issues between the responsibilities of EQC and those of private insurers.

Changes are needed to the EQC Act in order to embed lessons learned from Canterbury and other events

Fully responding to the concerns and lessons regarding EQC's performance and experiences requires a range of actions including making changes to the EQC Act. Amending the Act will ensure improvements are in place should a natural disaster event occur in the near-term.

Contents

This Regulatory Impact Statement (RIS) covers the following proposals:

- A time bar on reopening EQC claims (full impact statement).
- Monetary caps on retaining walls, bridges, and culverts (summary statement).
- Updating excesses for building and land cover (summary statement).
- Updating EQC's ability to provide insurer discounts (summary statement).

¹ Note subjective wellbeing in the context of the Treasury Living Standards Framework refers to wellbeing as reflected in people's own rating of their life, which can be considered to be 'life satisfaction'.

² By and large, claimants who participated in the Public Inquiry into EQC expressed dissatisfaction with the operational practices and outcomes of claims they experienced with EQC. See page 7 of the report of the Public Inquiry into EQC (2020): <https://eqcinquiry.govt.nz/assets/Inquiry-Reports/Report-of-the-Public-Inquiry-into-EQC.pdf>

- Clarifying what the Natural Disaster Fund can be spent on (summary statement).

Section 1: General information

Purpose

Treasury is solely responsible for the analysis and advice set out in this Impact Summary, except as otherwise explicitly indicated. This analysis and advice has been produced for the purpose of informing:

- *Final decisions to proceed with a policy change to be taken by or on behalf of Cabinet.*

Key Limitations or Constraints on Analysis

Policy

Ministers have directed officials to undertake a review of the EQC Act to modernise the legislation and embed lessons learned following the Canterbury earthquake sequence in 2010 and 2011. The 'modernisation' scope of the work means that a first-principles examination of the purposes and design of EQC has not been undertaken.

As a result, the following core features of the existing scheme and institutional arrangements were retained in all reform options:

- EQC cover being first-loss cover (that is, EQC takes the first loss in the event of a covered natural disaster, with the private insurer picking up losses beyond the EQC cover as required)
- access to EQC cover being compulsory for any residential building with a fire insurance policy
- EQC premiums being collected by private insurers and passed to EQC
- the EQC scheme being focused on only residential property
- separate EQC building and land cover, and
- EQC will continue to be a Crown Entity.

We consider that the above limitations did not impede the review of the EQC Act or addressing the relevant recommendations of the Inquiry.

Non-legislative options

These amendments are just one aspect of a package of legislative and non-legislative initiatives being progressed across government to implement recommendations of the Inquiry and embed lessons learned from the past.³ Most notably, EQC has already implemented a broad suite of operational improvements, including around how it works

3 The full Government response to the Public Inquiry into EQC, released in September 2020, is available here: <https://www.treasury.govt.nz/sites/default/files/2020-09/govt-response-eqc-inquiry-DEV-20-SUB-0116.pdf>

with claimants and private insurers to support timely, fair, and enduring settlements for Canterbury claimants and future events.

As part of these improvements, EQC is implementing an Insurer Response Model (IRM), which is a partnership between EQC and private insurers. Claimants will have one point of lodgement, assessment, and resolution for their insurance claims. EQC is ensuring all of its agents take a consistent approach to treating customers fairly, respectfully, and sensitively by developing an EQC Insurer Manual (as a core operational document for all parties performing claims management under the IRM). EQC is also developing a comprehensive assurance programme to support the IRM. This includes tracking insurer performance of Statement of Performance Expectation measures and customer feedback.

In addition to ongoing improvements in EQC operations, there are three main work streams across government that will take forward the various recommendations of the Public Inquiry into EQC:

1. A substantial modernisation of the EQC Act by the Treasury, with an amendment Bill to be introduced in 2021.
2. National Emergency Management Agency-led work on clarifying roles and responsibilities in the emergency management system.
3. A Department of Internal Affairs-led cross-government Community Resilience work programme, the overarching objective of which is to build community resilience to natural hazards and climate change risks.

This Regulatory Impact Statement (RIS) focuses on the first of the three workstreams. This workstream addresses matters raised in the Government's response to the Inquiry, and lessons from the Canterbury earthquake sequence that require legislative change to the EQC Act.

Criteria used to assess options

While there is no prescriptive set of arrangements that will be suitable for every entity, there are established principles and examples of good practice. The criteria used to assess options is specific to each of the issues covered in this RIS. We have generally not sought to establish formal weightings for these criteria, with the preferred option reflecting a judgement about which option is likely to best achieve an appropriate balance of the selected criteria.

We have not quantified the costs and benefits due to the difficulty of doing so in relation to:

- changes relating to matters of legislative design (i.e. clarifying what Natural Disaster Funds can be spent on), and
- data limitations.

Assessments reflect a judgement about the relative impact of options against the established criteria.

Data

The evidence base for this analysis has been drawn primarily from EQC claims data, EQC modelling, insurer-provided data, and stakeholder consultation. There are

limitations around the availability and quality of data on EQC insured property and claims.

Related Regulatory Impact Statements

This Regulatory Impact Statement (RIS) is one of four to support proposals to amend the EQC Act. A related RIS covering the EQC cap is being prepared in parallel to this RIS. Two additional RISs relating to modernising the EQC Act, and the treatment of mixed-use buildings under the EQC Act, have both been completed to a standard that meets the RIS quality assurance criteria. All RISs will be published on the Treasury website once the EQC Amendment Bill is introduced.

Consultation

There has been significant previous public consultation on issues with the current EQC Act and potential options for change in 2015, and during the Inquiry, which included extensive consultation with the people of Canterbury. Consequently, the Minister Responsible for the EQC decided not to undertake a full public consultation process, including with iwi/hapū, or to consult on an exposure draft of the proposed EQC Bill. The Treasury has instead undertaken a targeted consultation process with stakeholders on relevant proposals.

While the package of proposals to modernise the EQC Act does not propose fundamental reforms, the package is complex and technical in nature. The targeted consultation process does create a risk that groups not included in the targeted consultation could raise technical or other issues at Select Committee that officials had not previously considered. However, we do not think this presents a significant risk to any particular issue covered in this RIS.

Responsible Manager (signature and date):

Helen McDonald

Earthquake Commission Policy Team

Economic System Directorate

The Treasury

[April 2021]

To be completed by quality assurers:

Quality Assurance Reviewing Agency:

The Treasury.

Quality Assurance Assessment:

The Panel considers that the Regulatory Impact Statement **meets** the Quality Assurance criteria.

Reviewer Comments and Recommendations:

A quality assurance panel with representatives from the Regulatory Impact Analysis Team, Economic Policy Team and Macroeconomic and Fiscal Policy Team at the Treasury has reviewed the Regulatory Impact Statement (RIS) "EQC Act Technical Issues" produced by the Earthquake Commission Policy Team at The Treasury. This RIS is one of four to

support proposals to amend the Earthquake Commission Act 1993 (EQC Act). The Panel considers that it **meets** the Quality Assurance criteria.

This RIS covers the following technical issues identified in the EQC Act:

1. a time bar on reopening EQC claims
2. monetary caps on retaining walls, bridges, and culverts
3. updating excesses for building and land cover
4. updating Earthquake Committee (EQC)'s ability to provide insurer discounts
5. clarifying what the Natural Disaster Fund can be spent on.

The Panel notes that there was no public consultation on the options, which has created some risk that unexpected technical or other issues may be raised at the Select Committee stage. However, this risk is mitigated by the extensive consultation that took place during previous public consultation, the Public Inquiry and targeted consultation on the proposals. The RIS notes that while the public is likely to have an interest in increased excesses (Issue 3) the proposed excess amount is consistent with conclusions reached after considering the public consultation feedback on this issue.

The Panel further notes that the Treasury's recommended approach to Issue 1 differs with the proposal to be implemented by the EQC and the Minister responsible for the EQC.

Section 2: Problem definition and objectives

2.1 What is the policy problem or opportunity?

The EQC scheme supports access to affordable natural hazard insurance

Internationally, private markets for catastrophe insurance tend to be marked by low rates of insurance uptake and fluctuations in supply of this type of cover. This results in significant levels of under-insurance or non-insurance among homeowners.

Without something like the EQC scheme, many homeowners would not be insured against natural disaster risks. The experience elsewhere in the world is that, in that situation, governments provide ad hoc assistance to those homeowners after large natural disasters. This creates risks and uncertainty for homeowners, insurers and governments.

Through its “first loss” insurance scheme EQC gives New Zealanders access to affordable natural hazard insurance. The current scheme design has EQC taking on a lot of the risk (covering something like 85 per cent of the damage to housing from natural disasters). This contributes to high rates of insurance among New Zealand homeowners compared with other countries that face similar high risks from natural disasters. The scheme plays an important role in re-establishing local communities hit by natural disasters.

Additionally, through its research and education functions, EQC:

- improves knowledge and professional practices in order to reduce the Government’s liabilities from natural disasters and make communities more resilient to such events, and
- helps raise awareness of the ways individuals and communities can better protect their property. Stakeholders have expressed strong support for these educational activities.

Through its reinsurance/risk transfer function, EQC contributes to a better understanding of New Zealand’s risks by international reinsurers/international risk capital markets. EQC’s support of high-quality science and engineering research and practice also underpin New Zealand’s ability to assess risk and price it.

The EQC Act’s effectiveness was tested by the Canterbury earthquake sequence

The Earthquake Commission (EQC) provides natural disaster insurance cover for damage to privately insured residential properties. EQC plays a critical role in New Zealand’s ability to recover from natural disaster events. Recovery from natural disaster events supports New Zealand’s living standards across health, housing, safety and security, and subjective wellbeing domains.

The Public Inquiry into EQC

During 2010 and 2011, the Canterbury region experienced New Zealand’s most significant earthquake sequence in modern times. EQC received more than 583,000 claims for damage to approximately 168,000 residential dwellings from this event sequence. EQC’s response to the Canterbury seismic sequence has been subject to several reviews and inquiries, most notably the Public Inquiry into the Earthquake Commission (the Inquiry), chaired by Dame Silvia Cartwright, that reported in April 2020.

The EQC scheme's effectiveness was severely tested by the earthquake sequence in Canterbury:

- there was a lack of transparency around and clarity of the roles and responsibilities of EQC
- EQC's claims handling system was significantly overburdened, leading to negative experiences for claimants⁴
- this was exacerbated by a lack of understanding of, and mismatched expectations around, the claims handling and settlement process
- a lack of clarity and certainty around entitlements under the EQC Act including the scope of cover for both land and buildings, and
- boundary issues between the responsibilities of EQC and those of private insurers.

Neither EQC, nor the EQC Act, had been previously tested on an event the size of the Canterbury earthquake sequence. Concerns regarding EQC's response to this event have resulted in a number of reviews, including the Inquiry. The purpose of the Inquiry was to ensure lessons are learned from the Canterbury earthquake sequence and subsequent events, and that EQC has the appropriate policies and operating structure in place to ensure improved claims management experiences in the future.

The Inquiry found that, regardless of the views of the performance of EQC, New Zealand "is fortunate to have a natural disaster insurance scheme backed by the Government".⁵ The report produced a wide-ranging and comprehensive set of findings, resulting in 70 recommendations.

Modernising the EQC Act

The Inquiry identified a need to update the EQC Act across a range of areas. This included improved legislative clarity around key provisions and definitions in the EQC Act. Modernising the EQC Act is the focus of the proposals contained in this RIS, though we note that none of the proposals being advanced in this RIS were specifically recommended by the Inquiry. Rather, these issues have been identified as part of a broad review of the legislation, undertaken partly in response to the Inquiry's findings, but also to embed lessons learned from the Canterbury earthquake sequence and other disasters.

The package of proposals being put forward as part of the work programme to modernise the EQC Act will deliver on all recommendations of the Inquiry requiring change to the EQC Act. The proposals sit across this RIS and related RISs covering the EQC cap, modernising the EQC Act, and the treatment of mixed-use buildings under the EQC Act.

⁴ By and large, claimants who participated in the Public Inquiry into EQC expressed dissatisfaction with the operational practices and outcomes of claims they experienced with EQC. See page 7 of the report of the Public Inquiry into EQC (2020): <https://eqcinquiry.govt.nz/assets/Inquiry-Reports/Report-of-the-Public-Inquiry-into-EQC.pdf>

⁵ Page 58 of the report of the Public Inquiry into EQC: <https://eqcinquiry.govt.nz/assets/Inquiry-Reports/Report-of-the-Public-Inquiry-into-EQC.pdf>

2.2 Who is affected and how?

This RIS covers several topics that, taken together, will support the clarity, certainty, and durability of the scheme:

A time bar on reopening claims

EQC has advocated for a time bar on the basis that it will ensure that damage can be more easily attributed to an event and provide greater certainty to all parties. EQC advises that it becomes more difficult to attribute damage to an event, the longer after an event a claim is made. EQC advises that providing certainty to all parties in the system will mitigate the risks associated with an open-ended ability to reopen claims. This includes possible impacts on EQC's continued ability to secure reinsurance on reasonable terms, as well as potential pressure on the EQC levy.

The Treasury advised against the introduction of a time bar on reopening EQC claims. This is on the basis that the problems leading to reopened claims, including EQC processes and practices and poor assessments and repairs, are being addressed via other means, including through the Insurer Response Model. Related to this, a time bar has the potential to deprive property owners of their statutory entitlements where they are left with damaged properties, including where the damage is the result of the manner in which the claim was previously handled or settled.

The proposal would affect EQC claimants who would no longer be able to reopen claims 10 years from the date of the first settlement. EQC's former Claimant Reference Group (CRG) was consulted on the proposal. The CRG expressed concern that claimants who discover significant damage after the expiry of the time bar would be unable to access the funds necessary to undertake repairs.

The Insurance Council of New Zealand (ICNZ) considers "that the existing regime is appropriate" and does not support the proposed time bar.

Monetary caps on retaining walls, bridges and culverts

Replacing indemnity value with undepreciated value as the basis for determining the monetary cap for retaining walls, bridges and culverts ("land structures"),⁶ and introducing a fixed monetary cap for those caps, will ensure the EQC scheme provides cover for a large proportion of damage to land structures. This will also provide a clear point from which homeowners with more extensive land structures can buy private insurance top-up cover. EQC support the proposed changes. ICNZ agree to separate monetary caps being introduced for retaining walls, bridges and culverts in principle, in the interest of certainty, fairness and the sustainability of the regime.

The proposed changes to EQC cover for land structures will benefit the great majority of EQC claimants affected by the change by leading to higher value settlements for land structures.

Updating excesses for building and land cover, updating EQC's ability to provide insurer discounts, and clarifying what Natural Disaster Funds can be spent on

Updating excesses for building and land cover, clarifying what Natural Disaster Funds are spent on, and updating EQC's ability to provide insurer discounts, will make for a

⁶ Undepreciated value is the estimated cost of replacing the damaged structure with exactly the same structure, i.e. a like-for-like replacement. Indemnity value is calculated by depreciating that value. Therefore, the undepreciated value will always be larger than the indemnity value.

more equitable scheme, ensuring that the costs homeowners pay to access EQC cover are set at an appropriate level and used for appropriate purposes. Introducing measures to address these issues will support a more modern EQC Act which is in line with legislative best practice and encourage greater public understanding of and confidence in the EQC scheme (and in doing so, support social capital).

Moving from a percentage-based excess with a minimum and a maximum to a flat-rate excess for both building and land cover, means that lower-value building claims (the highest proportion of claims) will pay higher excesses than at present and some higher-value claims will pay lower excesses.

Updating EQC's ability to provide insurer discounts is opposed by insurers as it will remove some income insurers have previously received through collection of the EQC premium. However, it is rare for government agencies to remunerate private businesses that are required by law to collect levies on their behalf. This change aligns EQC levy collection with usual government practice.

Taken together, these changes support the durability of the EQC Act, as, if levy expenditure is perceived to be unfair or at odds with the purpose of the levy payment, or if excesses are set too high for insurance claims to be accessible, perceived fairness issues may arise for property owners, who ultimately are expected to cover the cost through EQC levies. This could lead to pressures to amend the Act (a durability issue).

2.3 What are the objectives sought in relation to the identified problem?

Taken together, the amendments have three overarching objectives:

1. enabling better community recovery following a natural disaster,
2. updating and improving the clarity and certainty of the role of EQC and the cover it provides, and
3. supporting the future durability and flexibility of the EQC Act.

The proposed changes covered in this RIS focus on supporting the clarity, certainty, and durability of the EQC Act in particular, and touch on several key parts of the EQC Act. This includes funding, design and the scope of the EQC scheme. The table below shows the specific and collective objectives that the proposals for each issue seek to achieve.

Issue	Proposal	Specific objective(s)	Relevant overarching objective(s) for modernising the EQC Act
Issue 1: A time bar on reopening EQC claims	A 10-year time bar on reopening claims, starting from the date of the first settlement. We note that the Treasury's preferred option is to maintain the ability of claimants to reopen EQC claims.	Provide claimants and EQC with a reasonable period of time in which to attribute damage to an event. Ensure certainty for all stakeholders.	Clarity and certainty of the EQC Act.

Issue 2: Monetary caps on retaining walls, bridges and culverts	Replacing indemnity value with undepreciated value as a basis for the valuing damaged retaining walls, bridges and culverts (“land structures”), and introducing a specified monetary cap (of \$50k for retaining walls and \$25k for bridges and culverts) for settlements based on undepreciated value.	Better aligning the scheme design with its policy goals and improving the scheme’s transparency and equity.	Clarity, certainty, and durability of the EQC Act.
Issue 3: Updating excesses for building and land cover	Increasing the \$200 minimum excess on building cover to \$500. Retaining the \$500 minimum and \$5000 maximum excesses on land cover. Discontinuing percentage-based excesses on building and land cover	Discourage low value/minor claims, while avoiding significant problems with affordability Improve simplicity and certainty of excess amounts prior to an event.	Clarity, certainty, and durability of the EQC Act.
Issue 4: Updating EQC’s ability to provide insurer discounts	Remove the legislative provision for insurer discounts.	Align with standard policy and legislative practice around collection of Crown levies.	Durability of the EQC Act.
Issue 5: Clarifying what the Natural Disaster Fund is spent on	Limit the NDF to be used to pay for direct insurance costs and any research or education that either provides an expected benefit to insured homeowners (i.e. levy holders) or reduces the costs of the scheme.	Improve transparency, flexibility, durability, accountability, and fairness.	Clarity, certainty, and durability of the EQC Act.

Section 3: Options identification

3.0 Policy proposals addressed in this impact statement

This impact statement is divided into three parts:

Part 1 includes full impact analysis on:

- **Issue 1:** A time bar on reopening EQC insurance claims.

Part 2 includes summary impact analysis on:

- **Issue 2:** Monetary caps on retaining walls, bridges, and culverts.
- **Issue 3:** Updating excesses for building and land cover.
- **Issue 4:** Updating EQC's ability to provide insurer discounts.
- **Issue 5:** Clarifying what the Natural Disaster Fund can be spent on.

Part 3 includes information on intended monitoring and evaluation arrangements across all topics.

Part 1: Full impact statements

- **Issue 1:** A time bar on reopening EQC insurance claims.

Issue 1: A time bar on reopening EQC claims

2.1 What is the current state within which action is proposed?

The EQC Act currently includes a statutory notification period,⁷ which places a time limit on when an initial claim must be notified by following an event. In contrast, once a claim has been lodged and settled, there is no time limit on a claimant’s ability to reopen a claim, for example, if further damage is later discovered. The Earthquake Commission Act 1993 (the EQC Act) does not distinguish between open, closed, and reopened claims.

EQC continues to receive large numbers of reopened claims relating to the Canterbury earthquake sequence. EQC categorises reopened claims as claims by property owners who have previously settled with EQC requesting reviews of their entitlements.

EQC currently receives around 450 – 600 reopened claims a month. 55% of reopened claims relate to missed damage, while 23% relate to issues with previous EQC repairs. All of the Canterbury earthquake sequence claims currently being managed by EQC are reopened claims, many of which have been reopened multiple times. 50% of all reopened claims are reopened by property owners who did not own the damaged property at the time of the original claim. On average, 40% of reopened claims go no further than the initial triage of a claim. Reasons for declining reopened claims include that EQC has already paid for the damage, EQC has paid up to the cap already, or that there is insufficient evidence to support the claim.

Claims handling and settlement and the claimant experience were important elements of the Public Inquiry into the Earthquake Commission (the Inquiry). The Inquiry noted that claims handling processes, poor assessments, inadequate scoping of work and poor repairs have led to ongoing issues for property owners and large numbers of reopened claims in relation to the Canterbury earthquake sequence.

Since the Canterbury earthquake sequence, and in response to the Inquiry, EQC has implemented a number of changes to its policies, procedures and organisational culture. Changes include the implementation of the Insurer Response Model⁸ and the preference for cash settlement as the default settlement approach. Both the Treasury and EQC agree that that these changes should significantly reduce the likelihood of reopened claims following a future event.

7 Claimants must notify EQC of a claim not more than three months after the damage occurred, or if this period has expired, not more than two years after the damage occurred. Where a claim is notified after the expiration of the three month period but within the two year period, EQC may decline the claim if the lapse of time before the notice was given materially prejudices the Commission’s ability to assess the claim. In both cases the notification period can be extended via regulation.

8 This refers to a contractual arrangement between EQC and private insurers whereby private insurers will take over claims handling and settlement of EQC claims.

2.2 What regulatory system(s) are already in place?

There are currently no time limits on reopening claims in the EQC Act. Claimants must notify EQC of damage within the statutory notification period. Claimants must then provide EQC with evidence to support the claim, as soon as practical after the damage is discovered, or as soon as the person is reasonably able to give notice. The Minister has also agreed to amend the existing information requirement provisions to further clarify that these apply on an ongoing basis, regardless of whether the claimant has previously settled with EQC.

Both the Limitation Act 2010 (Limitation Act) and the Building Act 2004 (Building Act) provide limitation periods as a defence to civil proceedings. ^[38]

The Limitation Act provides defendants with a defence where the claim is filed more than six years after the date of the action or omission on which the claim is based. There is also a late knowledge period of an additional three years, and a “long stop” period of 15 years.

2.3 What is the policy problem or opportunity?

The problem identified by EQC

EQC has identified two main problems associated with the current open-ended ability of claimants to reopen claims:

1. It becomes more difficult to attribute damage to an event the more time passes.
2. The status quo has resulted in a lack of certainty for all stakeholders in the EQC scheme, due to the ability of claimants to reopen claims on an indefinite basis. This may have an impact on reinsurance and the EQC levy.

Attributing damage to an event

It becomes more difficult for EQC and claimants to attribute damage to an event the more time passes. The longer the period since the event cover is being claimed for, the more difficult it will be to find evidence to support damage being related to a natural disaster event. This is compared to other causes such as age and maintenance. Additionally, when properties are sold, subsequent owners may not have the requisite level of knowledge to be able to attribute property damage to an event. EQC advises that reasons for damage being identified a long time after an event also include delays in owners commencing repairs, as well as the sale of properties where the previous owner has received a settlement but not repaired the property.

Certainty for all stakeholders

While there has been no impact on reinsurance appetite to date, the issue of re-openings is regularly discussed between EQC and reinsurers. EQC advises that there is the potential for reduced risk appetite from reinsurers should there be other significant loss paying events. As 70 - 80% of reinsurers in EQC's current reinsurance programme were part of EQC's programme at the time of the Canterbury earthquakes, the open-ended ability to reopen claims has had a direct impact on their exposure. This means they have needed to regularly increase their provisions in relation to the Canterbury earthquake sequence.

The lack of certainty also increases claims handling and settlement costs for EQC which must maintain the capacity to deal with claims on an ongoing basis. This may have a

flow on effect on the EQC levy as any increases in claims handling and settlement costs are taken into account when setting the levy.

The Treasury's view of the problem

The reasons why there were large numbers of reopened claims following the Canterbury earthquake sequence

As highlighted by the Inquiry, claims handling processes, poor assessments, inadequate scoping of work and poor repairs have led to ongoing issues for property owners. This has resulted in large numbers of reopened claims in relation to the Canterbury earthquake sequence. EQC data suggests that close to 80 percent of reopened claims relate to missed or failed repairs.

Operational changes at EQC have reduced the likelihood of reopened claims

EQC has taken steps to mitigate the likelihood of reopened claims following a future event. Changes include improvements to operational policies and procedures, the introduction of the Insurer Response Model and a preference for cash settlements. The Treasury anticipates that these improvements will significantly lessen the likelihood of claims being reopened following a future event.

2.4 What do stakeholders think about the problem?

Reopened claims and possible options for reducing the numbers of reopened claims were not consulted on in the 2015 discussion document. In addition, the Inquiry did not make any recommendations in relation to reopened claims. This means we have a limited understanding of the views of stakeholders on this issue.

We did consult with the Insurance Council of New Zealand (ICNZ) on the issue of reopened claims and options for reducing the number of reopened claims. ICNZ represents 28 fire and general insurance companies (including reinsurers). ICNZ noted that this is an extremely complex matter that cannot be fully considered in short timeframes. ICNZ observed as follows:

“In an ideal world, claims would not need to be reopened and there would be confidence that, if an EQC claim was closed (i.e. either by way of managed repair or cash settlement, with subsequent repairs completed), then the damage has been satisfactorily reinstated. Historically the reality was that in many cases claims were not effectively managed (and therefore not correctly settled) when they were first settled. This has been the causative issue driving issues for private insurers related to past events (not the fact that the claim has been reopened).”

In addition to consulting with ICNZ, we consulted with the former EQC Claimant Reference Group (CRG). The CRG was established in 2018 to provide feedback and advice on EQC claims handling and settlement. The CRG noted that some types of damage, for example, structural damage is difficult to discover. The CRG expressed concern that options intended to reduce the number of reopened claims may result in claimants who discover significant damage sometime after an event being unable to access the funds required to undertake repairs.

2.5 What are the objectives sought in relation to the identified problem?

EQC's objectives are to:

- provide claimants and EQC with a reasonable period of time in which to attribute damage to an event; and
- ensure certainty for all stakeholders.

These objectives need to be balanced against the wider objectives of the review of the EQC Act. In particular, in line with the Inquiry recommendations, the objectives of changes to the claims handling and settlement provisions have been to:

- improve the claimant experience; and
- support housing recovery and quality following a natural disaster.

Ensuring that damage can be attributed to an event

The further the period of time since an event, the more difficult it becomes for EQC and claimants to attribute damage to an event. The longer the period of time since an event, the greater the likelihood that claimants and EQC need to invest significant time and resources into identifying the cause of the damage.

Ensuring certainty for all stakeholders

Ensuring all stakeholders in the system have certainty regarding expectations with regard to when damage will be identified, claimed for and settled, will minimise some of the costs associated with the current open-ended ability of claimants to reopen claims. This may preserve the willingness of reinsurers to take on EQC risk and minimise any flow on impacts associated with claims handling and settlement for the EQC levy.

Improving the claimant experience

The Inquiry emphasised the importance of a people-centred approach to the handling and settlement of EQC claims. This includes the critical role of EQC in assisting populations to recover, particularly the most affected and vulnerable parts of the population. The need for fairness, certainty and timeliness emerged as important elements of the claimant experience.

Supporting housing recovery and quality following a natural disaster

Another theme of the Inquiry was the impact of natural disasters on a housing recovery. Housing recovery was identified as integral to the ability of communities to recover following a natural disaster. The quality of repairs was also an issue both in terms of the immediate recovery and the future resilience of the housing stock.

Option identification

3.1 What options are available to address the problem?

Option One: Status quo (the Treasury's preferred option)

The EQC Act currently includes a statutory notification period,⁹ which places a time limit on when an initial claim must be lodged by following an event. In contrast, once a claim has been lodged and settled, there is no time limit on a claimant's ability to reopen a claim, for example, if further damage is later discovered. The EQC Act does not distinguish between open, closed and reopened claims.

Since the Canterbury earthquake sequence, and in response to the Inquiry, EQC has implemented a number of changes to its policies, procedures and organisational culture. Changes include the implementation of the Insurer Response Model and the preference for cash settlement as the default settlement approach. These changes should significantly reduce the likelihood of reopened claims following a future event. In addition, as noted above, the Minister has agreed to amend the EQC Act to further clarify that the obligations on claimants to provide evidence to support their claims applies on an ongoing basis. The Treasury prefers this option on the basis that addressing the causes of reopened claims will substantially resolve the underlying problems. This approach is also most aligned with the objectives of the current review, relative to the other options.

While there is the potential for the unlimited reopening of claims to have an impact on reinsurance availability, that is not supported by current evidence or has not otherwise been demonstrated following the Canterbury earthquake sequence. Despite the large numbers of reopened claims associated with Canterbury, reinsurers continue to take on EQC risk. In addition, we note that any future reinsurance concerns could be addressed by retaining the status quo and introducing contractual time bars into EQC's reinsurance contracts.

Option Two: Time bar of 10-years starting from the date of the first settlement (EQC's recommended option, agreed to by the Minister Responsible for EQC)

This option would provide claimants with a 10-year period starting from the date of the first settlement in which to reopen a claim. The first settlement would be defined as outlined below.

To some extent, a 10-year time bar would align with the 10-year limitation period in the Building Act (albeit that the Building Act limitation period starts from the date of the act or omission). This suggests that a policy decision has been made in which 10 years has been identified as a reasonable period of time in which to identify building damage.

In terms of weighing up the different time periods for a time bar, we note that the shorter the time period in which claims may be reopened, the greater the likelihood that claimants will have unrepaired damage. The longer the time period in which claims may be reopened, the greater the likelihood that claimants will have the opportunity to reopen a claim and access the funds to undertake the necessary repairs. In addition, the longer

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Claimants must notify EQC of a claim not more than three months after the damage occurred, or if this period has expired, not more than two years after the damage occurred. In both cases the notification period can be extended via regulation.

the length of a time bar, the less likely it is that community concerns will prompt a government policy response, such as legislative amendments to the time bar

The first settlement would be the point at which an entire claim (including land and building claims) was settled. It is not currently defined in the EQC Act. The first settlement date is preferred by EQC as a starting point on the basis that while there would be different end dates for different claims depending on the time taken to settle, claimants would have the same period of time from the first settlement in which to reopen a claim .

A time bar would not override the limitation periods in section 11 of the Limitation Act [38]

A time bar would not apply retroactively (this also applies to Options three and Four). This means that it would not affect the rights of claimants whose claims arose from the Canterbury earthquake sequence, or any other natural disaster prior to the entry into force of an amended EQC Act.

In addition, a time bar would not remove the ability of claimants to bring legal proceedings or access dispute resolution mechanisms in relation to a claim, prior to and following the expiration of the time bar.

Option Three: Time bar of five years starting from the date of the first settlement

This option would provide claimants with a five-year time period in which to reopen their claims, starting from the date of the first settlement. EQC does not currently hold data on the number of claims reopened within five years of the first settlement as the concept of a first settlement is not defined in the EQC Act and has only recently been introduced to EQC's claims management systems.

A five-year time bar would apply prior to the six-year period in the Limitation Act and the 10-year period in the Building Act. A five-year time period would, therefore, increase the likelihood that claimants would lodge legal proceedings to reserve their position. There is also a concern that following a large natural disaster, a five-year time bar may not leave claimants with sufficient time to start repairs. As a consequence, claimants may have less time to identify damage that was not discoverable by non-invasive means.

Option Four: A time bar with exceptions in certain circumstances

A time bar on reopening claims could be subject to exceptions. For example, a time bar on reopening claims might not apply to claims where the natural disaster damage could not reasonably have been discovered in time to enable the insured person to claim for the damage; or the insured person is unable to give notice within the time period because of incapacity or other disability. A time bar with exceptions might be fairer to claimants who through no fault of their own could not reasonably have been expected to reopen a claim within the time bar period.

On the other hand, a time bar with exceptions also introduces an element of discretion to the application of the time bar. The exercise of this discretion introduces uncertainty and has the potential to result in inequitable outcomes where it is applied inconsistently. EQC advises that a discretion with regard to whether or not to apply the time bar also has the potential to result in additional administrative burdens. This is because it will require additional decision making regarding when the exception should apply.

3.2 What criteria, in addition to monetary costs and benefits have been used to assess the likely impacts of the options under consideration?

The following criteria have been used to assess the likely impacts of the options under consideration and have been weighted equally:

Claimants and EQC can attribute damage to an event

Both claimants and EQC should be able to attribute damage to an event. The EQC Act requires claimants to provide evidence of their claim, including that the damage is a direct result of a natural disaster. This becomes more difficult where damage is detected some time after an event.

Reinsurers continue to have a risk appetite for EQC risk

It is critical that reinsurers continue to have a risk appetite for EQC risk. The willingness of reinsurers to take on EQC risk ensures the ongoing viability of the EQC scheme. The EQC scheme relies on reinsurance to meet the costs of damage arising from natural disaster events.

The impact of claims handling and settlement costs on the EQC levy is managed

The impact of claims handling and settlement costs on the EQC levy should be managed to the extent appropriate. Claims handling and settlement costs are taken into account when setting the levy rate.

The likelihood of litigation does not increase

The Inquiry highlighted that the large volumes of litigation following the Canterbury earthquake sequence increased costs for all parties, prolonged the resolution of claims and introduced additional stress for claimants. The Inquiry made recommendations directed at reducing the likelihood of litigation following a future event.

EQC and insurer practice is aligned

The EQC Act review and operational changes at EQC have been intended to ensure greater alignment with private insurance. This will minimise the risk of claimants having to navigate dual systems following a future event.

Claimants can access the funds required to repair their homes

Following a future event, claimants should be able to access the funds necessary to repair their homes. Claimants have paid a premium for cover, up to the amount of the EQC cap. Claimants being able to access the necessary funds will support a housing recovery following an event.

3.3 What other options have been ruled out of scope, or not considered, and why?

A time bar starting from the date of the event or the date of the last settlement

Consideration was given to alternative starting points for a time bar. This includes a time bar starting from the date of an event.

A time bar on reopening claims starting from the date of the event may be difficult to implement in a situation like the Canterbury earthquake sequence where there was a series of insurable events. It could also result in claimants with simple claims that are settled quickly having more time to reopen their claim when compared to claimants with complex claims that may take more time to settle.

Consideration was also given to starting the time bar from the date of the last settlement. This was not preferred on the basis that each time a claim is reopened, the start date of the time bar is reset, resulting in claims that are reopened multiple times taking much longer to be finalised.

Making legislative provision for full and final settlements

Consideration was given to whether legislative provision needed to be made for EQC to settle claims on a full and final basis. A full and final approach to the settlement of claims would potentially mean that all claims relating to an event or a series of events would be closed earlier. This may reduce the administrative cost EQC is incurring in dealing with re-opened claims over time. A full and final settlement provision could also incentivise claimants to undertake due diligence.

On the other hand, a full and final settlement approach could result in claimants being more reluctant to accept a settlement, which could prolong the process. Full and final settlements would also mean that EQC would need to consider paying a 'contingency' to give homeowners a level of comfort that the settlement was sufficient for them to complete repairs, including for damage that might be discovered at a later date.

In addition, EQC does currently enter into full and final settlements on a discretionary basis. The High Court has confirmed that EQC can enter into full and final settlements in certain circumstances (see *He v EQC*)¹⁰.

Requiring a report from a Licensed Building Practitioner

EQC has previously advised that it has considered introducing minimum requirements to reopen a claim such as a Licensed Building Practitioner (LBP) report explaining why they consider it to be related to an event. This was one of a range of initiatives being considered by EQC to ensure its resources were focused on legitimate reopened claims.

This option has the potential to create additional costs for claimants. A LBP report may be unnecessary to demonstrate damage and the link to a natural disaster. It is not a requirement for making an EQC claim.

In addition, claimants are already required to provide evidence to support their claim. This obligation will be strengthened by the proposal to further clarify that the obligation applies on an ongoing basis.

¹⁰ [2017] NZHC 2136, at 120

Impact Analysis

Marginal impact: How does each of the options identified in section 3.1 compare with taking no action under each of the criteria set out in section 3.2?

	No time bar in conjunction with operational improvements at EQC and the implementation of the Insurer Response Model	Option: Ten-year time bar on reopening claims from date of first settlement	Option: Five-year time bar on reopening claims from date of first settlement	Option: A time bar with exceptions in certain circumstances
Criterion: Difficulties associated with attributing damage to an event are mitigated	0	+	++	+
		This option may address some of the difficulties associated with attributing damage to an event a long time after the event. This option provides claimants with a longer period of time in which to attribute damage to an event relative to a five-year time bar. This may mean that some of the claims presented near the expiry of the time bar may be more difficult to attribute to an event.	The closer the period in time to an event the claim is made, the easier it is for EQC and claimants to attribute the damage to the event. A five-year time bar on reopening claims would ensure that reopened claims can more readily be attributed to an event.	This approach could mitigate some of the difficulties associated with attributing damage to an event the longer after the event the claim is made. On the other hand, damage relating to claims that fit within one of the exceptions and, therefore, are not time barred, may be identified a long time after an event. In these cases, the same challenges associated with attributing damage to an event will likely apply.
Criterion: Reinsurers continue to have a risk appetite for EQC risk	0	+	+	+
		A 10-year time bar will provide reinsurers with certainty regarding the end point for reopened claims. This may maintain the willingness of reinsurers to take on EQC risk.	The Canterbury earthquake sequence demonstrated that a five-year time bar is a relatively short period of time in which to resolve all claims following a large event. This option would significantly reduce the period of time in which claimants could reopen claims. This would provide certainty to reinsurers that all claims will be settled in a relatively short period of time. The associated increase in litigation and associated increases in EQC's potential liability could reduce these benefits.	A time bar with exceptions might provide certainty to reinsurers. On the other hand, it will be difficult to anticipate the numbers of claims that would fit within the exceptions, reducing uncertainty.
Criterion: The impact of	0	+	+	0

claims handling and settlement costs on the EQC levy is managed		Claims handling and settlement costs associated with reopened claims would be reduced after the 10-year time bar takes effect. This could have a positive impact on the EQC levy.	Claims handling and settlement costs associated with reopened claims would be reduced after the five-year time bar takes effect. This could have a positive impact on the EQC levy. Any reduction in claims handling and settlement costs associated with a five-year time bar may be offset by the potential for increased litigation costs. We do not have enough evidence to make a definitive assessment on this point.	It is unlikely this option will reduce claims handling and settlement costs and hence the flow on effect for the EQC levy. A discretion in relation to a time bar has the potential to increase administrative burdens.
Criterion: The likelihood of litigation does not increase	0	- This option may increase litigation as claimants seek to reserve their position. However, the risk of increase is litigation is less than under the five-year time bar option.	-- This option is likely to increase litigation as claimants will be incentivised to lodge proceedings to reserve their position. This becomes more likely where, as here, the time bar precedes the time bar in limitation regimes.	-- This option is likely to increase litigation. Not only may claimants be incentivised to reserve their position, EQC advises that a discretionary approach may increase the likelihood of judicial review.
Criterion: EQC and private insurer practice is aligned	0	-- This approach does not align with insurer practice. It will create a new point of difference between the EQC scheme and private insurance, increasing the likelihood of a divergent response. This has the potential to create uncertainty and complexity for claimants.	-- This will create an additional point of difference between the EQC scheme and private insurance.	-- This will create an additional point of difference between the EQC scheme and private insurance.
Criterion: Claimants are able to access the funds required to undertake repairs	0	- The longer the period of time in which claimants may reopen claims, the greater the likelihood that they will be able to access the funds required to undertake repairs.	-- The Canterbury experience has shown that following a large event, it may take time to identify and claim for damage. In addition, the manner in which a settlement is dealt with may mean that claimants are left with unrepaired homes following a settlement. This option increases the likelihood that these claimants may be unable to access the funds required to undertake repairs.	- The impact of a time bar on the ability of claimants to access the funds required to undertake repairs may be minimised where exceptions are made. Where the exceptions are restricted to the fault of other parties, this may mean that difficult to discover damage or other damage not subject to the exceptions is not repaired.
Overall assessment	0	-	--	---

Key:

- ++** much better than doing nothing/the status quo
- +** better than doing nothing/the status quo
- 0** about the same as doing nothing/the status quo
- worse than doing nothing/the status quo
- much worse than doing nothing/the status quo

Conclusions

5.1 What option, or combination of options is likely to best address the problem, meet the policy objectives and deliver the highest net benefits?

The Treasury's preferred option is to retain the status quo. We note that EQC's preferred option is a time bar on reopening EQC claims, which has been agreed to by the Minister Responsible for EQC. This is reflected in the analysis, including the assessment of the options against the decision-making criteria.

Retaining the status quo will support the wider objectives of the EQC Act review

We recognise that the open-ended ability to reopen EQC claims has created administrative burdens for EQC. Our view, however, is that changes underway to EQC's claims handling and settlement practices, are an appropriate mechanism for ensuring that claims are settled in a fair, timely and enduring way following a future event. This will lessen the likelihood of large numbers of claims being reopened several years later.

The analysis above demonstrates that there are a number of advantages and disadvantages associated with the options considered. There is a balance to be struck between:

- managing the difficulties associated with attributing damage to an event and the lack of certainty associated with the open-ended ability to reopen claims; and
- improving the claimant experience and supporting a housing recovery.

The status quo aligns with the wider EQC Act review objectives to improve the claimant experience and support a housing recovery following a natural disaster. The status quo will not increase the volume of litigation relative to a time bar. In addition, it aligns with private insurance practice, ensuring ongoing clarity and reduced complexity relative to the alternative options. The status quo ensures that claimants are able to access their statutory entitlement up to the amount of the cap. This includes where there are issues with claims handling and settlement practices, or damage is difficult to discover following a future event.

A time bar on reopening claims will assist with managing difficulties associated with attribution of damage and a lack of certainty

EQC's preferred option is a 10-year time bar on reopening EQC claims starting from the date of the first settlement. This has been agreed to by the Minister Responsible for EQC.

The proposed time bar will reduce administrative burdens for EQC and claimants associated with attributing damage to an event the longer the period of time since the event occurred.

In addition, the ability to reopen claims has created uncertainty for all parties. EQC advises that this uncertainty may reduce reinsurers ongoing willingness to take on EQC risk. It could also have an impact on the EQC levy.

A five-year time bar starting from the date of the first settlement has been assessed against the decision-making criteria as more likely to meet EQC's policy objectives. However, when balanced against the wider objectives of the EQC Act review, a 10-year time bar starting from the date of the first settlement is the preferred alternative to the

status quo. This is when compared to the other two alternative options to the status quo considered as part of this analysis.

What do stakeholders think?

As noted above, we have a limited understanding of the views of stakeholders on this issue. We did consult ICNZ and the CRG on the options for limiting reopened claims. This issue was not consulted on in the 2015 public consultation. The Inquiry did not recommend a time bar on reopening claims.

ICNZ does not support a time bar and considers “that the existing regime is appropriate in this regard”. ICNZ notes that this is an extremely complex matter that cannot be fully considered in short timeframes and observed as follows:

“We do not understand how this could work. Specifically:

- *Private insurance claims are subject to limitation periods under the Limitation Act 2010 and the operation of section 9 of the Insurance Law Reform Act 1977.*
- *Introducing the time bar for EQC claims could lead to a divergent response in so far as the claim was, or became, over cap as acknowledged in paragraph 12 of the proposal document. Private insurers could find themselves in a situation where we need to deal with multiple different time bars for the same claim event. In this situation there is potential for the EQC claim component to be time barred while the private insurer component is not (or vice-versa).*
- *This proposal would also likely result in poor customer outcomes (e.g. they could be left in a position without the necessary funds to reinstate their house). This may also lead to reputational issues for EQC and pressure being placed on the private insurer to meet costs that would have been met by EQC had the claim not been time barred.*
- *A divergent outcome would also cause additional complexity and claim management costs for private insurers.*

The introduction of a new time bar may also, counter-intuitively, precipitate more litigation, including potential class action or claims involving advocates as customers find themselves under time-bound pressures to make the strongest case via adversarial / litigious means rather than an orderly resolution via the standard claims process. A time bar that sees the clock start running upon settlement may see EQC claim lifecycles prolonged with customers being less comfortable to accept settlement. Again, this may lead to more advocate involvement.”

The CRG noted that some types of damage, for example, structural damage is difficult to discover. The CRG expressed concern that claimants who discover significant damage after the expiry of the time bar will be unable to access the funds necessary to undertake repairs.

We also consulted the Legislation Design and Advisory Committee (LDAC) who provided advice on the proposed time bar and its features, including the following¹¹:

“Is the purpose of the time bar clearly defined and discernible?”

1. *As discussed at the meeting, LDAC advises EQC and Treasury to think carefully about the objectives of the proposed time bar on the reopening of claims. What is the exact problem that this proposal aims to solve?*

¹¹ Letter from LDAC to the Treasury regarding the review of the Earthquake Commission Act 1993, 22 April 2021

2. *It is important that the policy objective of the time bar is clearly articulated and the provision designed to meet that objective.*¹²
3. *The time bar proposal was not consulted on in the 2015 discussion document and was not a recommendation of the Inquiry.*¹³ *The objectives of the time bar are set out in the Treasury Report as:*
 - a. *Addressing difficulties in attributing damage*
 - b. *Increasing certainty for all stakeholders.*
4. *The “primary driver is addressing difficulties in attributing damage.”*¹⁴
5. *As discussed, there are four obvious circumstances in which claims are reopened:*
 - *damage was not repaired properly; or*
 - *EQC has not properly discharged its responsibilities under the Act; or*
 - *the homeowner has discovered additional damage; or*
 - *damage has been incremental.*

EQC may be able to identify other categories of reopened claims.

6. *Is a time bar consistent with efficiently responding to issues raised by all these types of reopened claims? What is the legal effect of the proposal on EQC’s duties and on the legal rights of claimants?*
7. *For instance, in cases where damage was attributed to a disaster but not repaired properly, how does a time bar meet the primary objective of not reopening claims at a time when it is difficult to identify the cause of the damage? As currently proposed, the time bar would apply to claims where damage has not been repaired satisfactorily due to institutional failures at EQC. It is difficult to see why a claimant should be time barred from having such a claim reopened.*

Would a time bar be consistent with the policy objectives and purposes of the legislation?

8. *The provisions of the proposed legislation should be consistent with its purpose and the policy objective that underlies it.*¹⁵ *The time bar should also be consistent with the overall objectives of the new legislation. We note, for instance, that the Inquiry identified as an issue fairness in the way claimants are treated and that the review of the EQC Act responds to the Inquiry. LDAC is concerned that the time bar may artificially cut off an administrative avenue for dealing with legitimate issues. Instead, claimants may be forced to commence proceedings to enforce their rights. Litigation is unlikely to be an efficient mechanism for dealing with these issues.*

¹² Legislation Guidelines (2018 edition) chapter 2.1. The policy objective should be clearly defined and discernible.

¹³ Treasury Report: Modernising the Earthquake Commission Act: Claims Handling and Settlement – Additional Issues, 24 February 2021, at paragraph 34.

¹⁴ Treasury Report: Modernising the Earthquake Commission Act: Claims Handling and Settlement – Additional Issues, 24 February 2021, at paragraphs 18 and 19.

¹⁵ Legislation Guidelines (2018 edition) chapter 2.2.

Is legislation needed to give effect to the policy objective?

9. *Are there more appropriate ways of solving the problem that do not raise the same concerns? In particular, LDAC recommends that EQC and the Treasury think carefully about whether legislation is needed at all. Legislation should only be made when it is necessary and is the most appropriate means of achieving the policy objective.¹⁶*
10. *Are there non-legislative/administrative changes that could be made to EQC’s claims settlement process that would more effectively address the issue? If the time bar is not intended to compromise claimants’ rights to take legal proceedings, it would appear that the time bar is primarily aimed at addressing an administrative issue relating to whether EQC should re-assess a claim. If that is the case, a 10-year time bar appears to be a rather blunt mechanism for dealing with an administrative issue.”*

While we did not consult the New Zealand Bankers’ Association (NZBA) on the proposed time bar, we did receive feedback from one of its members, the Bank of New Zealand (BNZ), in relation to an earlier proposal to make legislative provision for full and final settlement (refer to section 3.3). The consultation material listed the alternative options of a time limit on reopening claims, or changing the threshold for reopening claims. BNZ provided the following comments:

“BNZ considers it is important to preserve these rights. We are aware of a number of cases where properties had been repaired and quite some time later it was discovered that the repairs were not up to standard or inadequate. Same with missed damage.

BNZ considers that some actions can assist in this area, such as:

- *-A time limit on reopening claims (Option 3)*
- *-EQC & Insurers using approved engineers, quantity surveyors/valuers, loss adjusters and repairers that guarantee their work.*
- *-Clear criteria for when a claim can be reopened (Option 4)*
- *-Notification to banks who have a financial interest in insured properties should a claim be reopened and/or settled”.*

5.2 Summary table of costs and benefits of the preferred approach

Affected parties (identify)	Comment: nature of cost or benefit (eg, ongoing, one-off), evidence and assumption (eg, compliance rates), risks	Impact <i>\$m present value where appropriate, for monetised impacts; high, medium or low for non-monetised impacts</i>	Evidence certainty (High, medium or low)

¹⁶ Legislation Guidelines (2018 edition) chapter 2.3.

Additional costs of proposed approach compared to taking no action			
EQC	The proposed time bar has the potential to reduce claims handling and settlement costs for EQC associated with reopened claims.	Low	Low
Private insurers	Private insurers have advised that a time bar on reopening claims would increase complexity and claims handling costs. This includes costs associated with: multiple time bars relating to the same event; pressure being placed on private insurers to meet the costs that would have otherwise been covered by EQC; and the potential for more litigation.	High	Medium
Insured homeowners	Homeowners may not be able to access their full statutory entitlement in the period where damage is not easily detected. This includes where the damage is the result of faulty repairs or missed damage as part of an EQC assessment. The extent to which this may be an issue will depend on the event and the response to the event. In addition, homeowners may feel obliged to reserve their position via lodging court proceedings. This may increase costs for claimants.	Medium	Low
Total Monetised Cost	Not available.	Not available.	
Non-monetised costs	A time bar on reopening claims may reduce the claims handling and settlement costs for EQC associated with reopened claims. A time bar on reopening claims may increase costs for the insurance industry and homeowners.	Medium	Low

Expected benefits of proposed approach compared to taking no action			
EQC	A time bar on reopening claims would reduce the administrative burdens for EQC associated with reopened claims. Efficiency gains may be mitigated if the time bar increases the volume of litigation. We have insufficient evidence to be able to make a definitive assessment of the extent to which the proposed time bar will reduce administrative burdens for EQC.	Medium	Low
Private insurers	There are some disadvantages associated with reopened claims	Low	Medium

	for insurers, including not seeing some over cap claims until sometime after an event. A time bar may provide limited benefits to insurers by lessening the likelihood of this occurring. We note that when assessed against the potential costs to the insurance sector, private insurers prefer the status quo.		
Insured homeowners	Homeowners may be incentivised to more promptly identify damage and may find that it is easier to attribute damage to an event. Some damage is difficult to discover and post-Canterbury, many issues leading to reopened claims including failed repairs and missed damage were not the fault of the claimant.	Low	Low
Total Monetised Benefit	Not available.	Not available.	
Non-monetised benefits	A time bar on reopening claims would reduce complexity for EQC leading to a reduction in administrative burdens. A time bar on reopening claims would have minimal benefits for insurers and homeowners.	Low	Low

5.3 What other impacts is this approach likely to have?

The current system provides flexibility. The large numbers of reopened claims arising out of the Canterbury earthquake sequence can in part be attributed to the nature of the event and the form of the response. Should a different set of problems arise following a future natural disaster event, government intervention may become necessary. This could involve a legislative amendment to the time bar. It could also include some sort of ex gratia package to assist affected homeowners.

A time bar on reopening claims may have a disproportionate impact on vulnerable homeowners. Examples include people with poor eyesight or the elderly, who may struggle to identify damage within the requisite period. The types of vulnerabilities where this may arise as an issue is fairly broad. It is difficult to assess the likely impacts on vulnerable groups in advance of an event occurring. EQC advises that it has systems in place to ascertain claimants' vulnerabilities and respond accordingly.

EQC has noted that the proposed time bar should support a better community recovery overall. Damage would be identified and claims resolved within the prescribed period of time. It is difficult to predict or measure to what extent this might be the outcome of a time bar on reopening claims in advance of an event.

Part 2: Summary impact statements

- **Issue 2:** Monetary caps on retaining walls, bridges, and culverts.
- **Issue 3:** Updating excesses for building and land cover.
- **Issue 4:** Updating EQC's ability to provide insurer discounts.
- **Issue 5:** Clarifying what the Natural Disaster Fund can be spent on.

Issue 2: Monetary caps on retaining walls, bridges, and culverts

3.2 What options have been considered?

Status Quo - Purpose and Current Design of EQC land cover

EQC¹⁷ land cover was introduced following the 1979 Abbotsford landslide, which destroyed 69 houses, and their associated land, in Dunedin. The then-EQC scheme paid out for the destroyed houses, but not the associated land. The resulting Royal Commission recommended an extension of EQC cover for “loss of use of land”.

The Royal Commission's support of land cover was based on political economy and policy coherence arguments. The Royal Commission noted that the scheme should meet “the reasonable expectations of the public” and that the then-EQC scheme represented a policy choice that the state insure otherwise-uninsurable disaster risks. Land damage that results in loss of use of the land in reinstating damaged housing was considered to be such a risk.

The core policy purpose of EQC land cover is clear; to compensate residential property owners for damage to land that protects and supports the affected residential building and access to the building. If an affected land holding is uneconomic to repair, the land cover provides sufficient compensation to enable the affected owner to buy land of similar quality to that which has been lost (albeit based on the smallest land area permitted under the relevant local district plan).

The coverage provided under the current Act largely achieves this.

In contrast to residential buildings, private insurers do not insure land. Therefore, any land damage losses not met by EQC will fall on the affected property owner. Private insurers do however insure some structures covered by EQC land cover, namely retaining walls, bridges and culverts (collectively referred to as “land structures” in this report).

EQC land cover insures “residential land” as defined in the EQC Act:

“Residential land means, in relation to any residential building, the following property situated within the land holding on which the residential building is lawfully situated:

- (a) the land on which the building is situated; and
- (b) all land within 8 metres in a horizontal line of the building; and
- (c) that part of the land holding which—

¹⁷ Prior to 1994 the Earthquake Commission was the Earthquake and War Damage Commission. For narrative simplicity when referring to either organisation, and their schemes, we use the term EQC throughout this document.

- (i) is within 60 metres, in a horizontal line, of the building; and
 - (ii) constitutes the main access way or part of the main access way to the building from the boundary of the land holding or is land supporting such access way or part; and
- (d) all bridges and culverts situated within any area specified in paragraphs (a) to (c); and
- (e) all retaining walls and their support systems within 60 metres, in a horizontal line, of the building which are necessary for the support or protection of the building or of any property referred to in any of paragraphs (a) to (c).”

EQC land cover will currently pay up to:

- the value, at the site of the damage, of an area of land that is the smallest of:
 - a the area of land that is actually lost or damaged, or
 - b the minimum section area allowable under the relevant local authority District Plan, or
 - c 4,000 square metres (m²) of land,

(the land area rules of EQC land cover are not considered further in this analysis, which focuses on the rules applicable to land structures), plus
- the indemnity value of any damaged retaining walls, bridges or culverts that form part of the residential land.

The land and land structure settlement forms one pool, so settlement monies from land damage that are not directed to land reinstatement may be devoted to reinstating land structures, and vice-versa. EQC’s obligation is to fund the repair of the damaged land or land structures, up to the applicable dollar/ value caps. The practical effect of this is that EQC currently usually pays the lesser of:

- the actual or estimated cost of repairing the damaged structure, and any associated land, or
- the indemnity value of the damaged structure, plus the market value of any associated damaged land.

When land structures are damaged, the most common land remediation solution is to replace or reinstate the damaged land structure.

EQC land cover is separate from EQC building cover. Unlike EQC building cover, EQC land cover has no fixed monetary cap. The maximum value entitlements are determined by the value of the relevant land areas described above (plus the indemnity value of any damaged land structures).

Problem Definition

The use of a monetary cap based on the indemnity valuation of the particular damaged land structure raises three issues of policy concern:

- The indemnity value cap can result in payments that are insufficient to reinstate or replace the damaged structure. That is inconsistent with the policy intention. This is most likely when the land structure is older, and so largely depreciated, and when the associated damaged land is of relatively low value, and so makes a relatively modest contribution towards costs of repairing the damaged land structure.
- Reinstatement or replacement of land structures, especially large or complex retaining walls, can be very expensive (settlements can be for several hundred thousand dollars). This raises equity issues (noting EQC land cover is not separately priced through levies) and raises policy issues regarding appropriate risk sharing between EQC, homeowners, and private insurers.
- Indemnity values are not known in advance of a claim, so are not clear, certain, and transparent. This means homeowners can only estimate their level of EQC cover for these structures, making it difficult for homeowners to make informed choices regarding the purchase of further top-up cover for these structures from private insurers.

Decision-making criteria

The decision criteria are better aligning the scheme design with its policy goals and improve the scheme's transparency and equity.

During the policy development process the responsible Minister determined, on advice, that the Government's policy interest regarding EQC land cover is that it:

- contribute resources to reinstate or replace land damaged by natural disaster where that land contributes to providing support and protection for a residential building, and/ or the main accessway to the building, and,
- if it is not practicable to replace or reinstate a residential building on the affected land, provide resources to help contribute to the land-related costs of establishing another residential building elsewhere.

Options considered

We considered four options to reform the monetary caps applicable to land structures:

- The status quo (namely, valuing damaged land structures at their indemnity (depreciated) value);
- Valuing damaged land structures at their undepreciated value (namely, on the basis currently used to calculate the initial when-new starting value of the damaged land structure, which currently is then depreciated to determine the indemnity valuation);
- Valuing damaged land structures on their replacement value (namely, the cost to replace the damaged land structure to current standards, that is, modified as necessary to comply with any applicable laws).
- Introducing a maximum monetary cap. In effect, this is a supplementary option available for any of the above options.

As noted in the earlier section "Status Quo - Purpose and Current Design of EQC land cover", EQC currently usually pays the lesser of:

1. the actual or estimated cost of repairing the damaged structure, and any associated land, or

2. the indemnity value of the damaged structure, plus the value of any associated damaged land.

All these options retain this broad structure, so EQC would pay the lesser of the cost of repairing the damaged structure, and any associated land, up to the value of the damaged structure under the relevant option (indemnity/ depreciated/ replacement/ monetary cap), plus the value of any associated damaged land.

Options analysis

Status Quo- indemnity (depreciated) value

Retaining the status quo would not address the issues identified in the problem definition. It is the option with the lowest cost of claims for EQC.

Undepreciated value

Undepreciated value is the estimated cost of replacing the damaged structure with exactly the same structure, i.e. a like-for-like replacement. Indemnity value is that value after deducting depreciation. Therefore, the undepreciated value will always be larger than the indemnity value. This change would significantly advantage EQC claimants where the indemnity value (rather than repair cost) is currently the limiting factor of the settlement, while commensurately increasing the costs of affected EQC settlements. The gap between undepreciated and indemnity values is often very large, particularly for older land structures.

Officials' recommend this option, in conjunction with a maximum monetary cap.

Replacement value

Replacement value is the estimated cost of fully reinstating a damaged structure using solutions acceptable today. Replacement value is usually larger than undepreciated value. This is because usually, in the case of land structures, a new replacement structure will be more substantial, and hence expensive, than the structure that failed. This is in part due to regulatory and engineers' professional standards increasing over time, and in part because land structures that generate EQC claims are not randomly selected – poorly built or under-engineered structures are more likely to fail and generate a claim than more sturdy structures are.

Officials recommend against replacing the indemnity value cap with a cap based on the replacement value. This approach would lead to perverse and inequitable outcomes as EQC would fully fund replacement of poorly built (and relatively low-cost) structures with properly built and engineered ones.

Maximum Monetary Cap

A maximum monetary cap is akin in concept to the monetary cap on EQC building cover. Under this option, EQC's maximum settlement for damaged land structures would be capped at an explicit dollar limit, for instance \$50,000. This would limit an EQC settlement to that dollar amount, if the estimated or actual repair costs, or the value of the damaged land structure under the chosen valuation methodology, exceeded the monetary cap.

If only the change to undepreciated or replacement value were made, EQC cover would meet a large fraction of the reinstatement or replacement costs of very expensive and substantial structures. As EQC premiums (set for building cover and not for land cover) are flat-rate, and do not reflect property-specific risks regarding sometimes-expensive

land structures, this would raise equity concerns within the scheme, and reduces incentives on owners of those structures to consider and manage the ownership obligations and financial risks they pose.

Therefore, officials recommended that the shift from indemnity value to undepreciated value caps be accompanied by the introduction of a fixed monetary cap.

Choosing a monetary value for the cap

Regarding the actual monetary values for the proposed caps, the key policy aims are to:

- (a) provide cover for a large proportion of damage to land structures within the EQC monetary cap, and
- (b) provide a clear point from which homeowners with more extensive land structures can buy private insurance top-up cover.

Therefore, officials recommend a fixed monetary cap which fully captures a large fraction of EQC's expected land structure claims. Fixed monetary caps would align the design of this cover more closely with EQC building cover, and private insurer cover for land structures.

Based on EQC's claims data and analysis, summarised below, officials proposed a monetary cap on EQC retaining wall cover of \$50,000 per dwelling, and a monetary cap on cover for bridges and culverts of \$25,000 per dwelling (both amounts excluding GST).

These amounts are substantially more than the 95th percentile of estimated indemnity values for both retaining walls and culverts, and the 80th percentile for bridges, circled in Table 1 below. Therefore, the proposed monetary caps would be a significant improvement in cover, compared to the status quo, for the great majority of EQC claimants where the current indemnity value is the limiting factor on their claim.

This data needs to be interpreted with caution. It is based on small samples of claims (about 60 retaining wall claims, 30 bridge claims and 30 culvert claims). The percentiles are based on fitting an assumed log-normal distribution to those samples. Lastly, it uses repair cost as a proxy for undepreciated value (is not recorded by EQC). Repair cost will likely over-estimate undepreciated value of retaining walls (as the replacement retaining walls is often more substantial and expensive than the one that failed) and under-estimate undepreciated value of bridges and culverts (as damage to bridges and culverts often involves damage to the land supporting the bridge e.g. undermining the bridge abutments and/or damage to non-structural elements e.g. rails and planking. Such damage is relatively economical to repair (e.g. by placing gabion baskets (wire baskets of rocks) around the abutments to prevent further scouring and reinforce the structure.

These proposed caps would apply per EQC-insured dwelling. Therefore, a residential building with multiple dwellings would be entitled to multiple monetary caps.

Table 1: Estimated values of specified percentiles of (GST-exclusive) retaining wall, bridge and culvert indemnity values and repair costs

Percentile	Retaining Walls		Bridges		Culverts	
	Indemnity value (status quo)	Repair cost	Indemnity value (status quo)	Repair cost	Indemnity value (status quo)	Repair cost
50 th percentile	\$8,000	\$33,000	\$10,000	\$13,000	\$2,000	\$6,000
60 th percentile	\$10,000	\$41,000	\$13,000	\$16,000	\$3,000	\$7,000
70 th percentile	\$12,000	\$52,000	\$17,000	\$20,000	\$4,000	\$9,000
80 th percentile	\$15,000	\$68,000	\$23,000	\$27,000	\$6,000	\$12,000
90 th percentile	\$22,000	\$100,000	\$36,000	\$41,000	\$9,000	\$18,000
95 th percentile	\$29,000	\$136,000	\$52,000	\$58,000	\$12,000	\$25,000

Periodic Review

The Government intends that in future, EQC’s key financial settings, including the insurance premium and EQC insurance cap, should have a maximum review period of five years. Officials propose that the monetary caps for land structures be subject to the requirement to be reviewed at least every five years.

3.2A Which of these options is the proposed approach?

The Government proposes that indemnity value monetary caps for land structures be replaced by undepreciated value, up to a monetary cap of \$50,000 (excluding GST) for retaining walls, and \$25,000 (excluding GST) for bridges and culverts.

The “undepreciated value” option considered the best option as it improves settlement outcomes for the great majority of affected EQC claimants consistent with the problem definition, while also avoiding incentive and equity concerns associated with the “replacement value” option.

The monetary caps limit the benefits of EQC cover of expensive land structures and provide a clear dollar value departure point from which owners of properties with expensive land structures may choose to purchase further top-up cover for those items from private insurers. This improves the overall equity of the scheme, especially as land cover is not priced separately from EQC building cover. The proposed changes also support the clarity, certainty, and durability of the EQC Act.

The preferred option reduces, but does not eliminate, differences between the structure of EQC building cover and the structure of EQC cover of retaining walls, bridges and culverts. As proposed, both covers would pay the actual (or estimated) cost of repair, up to a defined dollar cap.

Compared to EQC building cover, the proposed EQC cover for land structures includes the additional limitation that the EQC settlement payment for the damaged structure not exceed the undepreciated value of the structure. The primary purpose of this limitation is so the EQC payment for the land structure reflects the value of the damaged structure. Aside from being inherent in the “indemnity” approach that applies to EQC land cover generally, i.e. including damage to land itself, it also protects against EQC funding expensive fully engineered solutions to originally inadequate structures. Land structures, particularly retaining walls, can vary widely in quality and appropriateness for the task.

Compared to the status quo, both removing depreciation from the calculation of EQC entitlements for land structures, and introducing a monetary cap, reduce the differences between EQC cover for buildings and land structures. This is because settlements based on undepreciated value will result in larger settlements than those based on depreciated value.

Issue 3: Updating excesses for building and land cover

3.3 What options have been considered?

Status quo

The excess amounts, set by regulation, are what claimants must pay if they decide to make a claim. The primary purpose of an excess is to help prevent large numbers of low value/minor damage claims from consuming limited claims handling capacity.

Existing EQC claims excesses (GST inclusive) are:

- for a residential building claim: \$200 multiplied by the number of dwellings in the building (e.g. in the case of an apartment building), or 1% of the settlement amount, whichever is greater. As EQC building cover is currently capped at \$150,000 (GST exclusive) per dwelling, the maximum excess on a building claim for a single dwelling is \$1,725 (GST inclusive).
- for a residential land claim: \$500 multiplied by the number of dwellings in the residential building which is situated on the land, or 10% of the settlement amount, whichever is greater, to a maximum of \$5,000.

Problem definition

The land cover excess was introduced in 1993 and the building excess amounts, set in 1984, pre-date the current 1993 Act. If the building claim excess is not changed, low value/minor building claims will increasingly consume limited claims handling capacity.

Excesses that are based on a percentage of the claim value add unnecessary complexity and create uncertainty for customers and EQC, as the excess cannot be calculated until a claim is finalised. Also, the excess may change if a claim is reopened.

Some claimants, particularly those on fixed/low incomes, may struggle to pay the maximum excess amounts where these apply, particularly:

- the \$5,000 land cover excess when applied to stand-alone dwellings; and
- the building cover excess for larger multi-unit buildings (MUBs), where the maximum excess can be hundreds of thousands of dollars (i.e., much larger than necessary to discourage minor claims). For example, the current maximum excess for building claims for a 12-storey building containing 100 dwellings is \$172,500 (GST inclusive). If the proposed \$500 excess is agreed, the building excess for a 100 apartment MUB would be \$50,000 (being \$500 x 100 apartments).

An excess set too high could mean that some repairs are not completed or are completed to a standard lower than existed prior to the damaging event.

Decision-making criteria

The key criteria applied to the option analysis were that the excess amounts should be:

- sufficient to discourage low value/minor claims for different types of residential buildings and land (a key efficiency concern relating to the consumption of limited claims handling capacity);

- not so high as to create significant problems with affordability and/or cost-cutting that results in incomplete or poor-quality repairs (a key recovery concern);
- relatively simple to calculate; and
- known at the time insurance cover is purchased (i.e., prior to making a claim).

Officials also considered the reduction in the real value of the excesses since they were first established. The \$200 (GST inclusive) minimum excess for building claims was established in the Earthquake and War Damage Regulations 1984. If the \$200 minimum excess on EQC building cover were adjusted for CPI inflation it would be well over \$600.¹⁸

Options considered

Officials considered excesses ranging from \$500-\$2,000, as well as the status quo.

The table below, based on EQC modelling completed in January 2021, shows the impact of different flat rate building claim excesses on EQC claim numbers and costs based on a Wellington earthquake reference event.¹⁹ The table does not account for land claims as EQC systems do not enable this to be considered.

Table: Impact of different building claim excesses for reference event

Excess on building claims	Reduction in reference event number of EQC building claims	Reduction in average annual claims \$ million	Reduction in reference event expected liability \$ million
\$500	2.8%	1.2	5
\$1,000	6.0%	4.1	81
\$2,000	10.5%	9.3	228
\$5,000	21.3%	21.6	637

While judgements may vary regarding the appropriate level of the excess (\$500 versus \$1,000 etc), officials consider that moving to a flat-rate excess, and discontinuing the percentage-based excesses, would significantly simplify claims handling and improve claimant understanding of their EQC entitlements. Submissions on the 2015 discussion document proposal for a \$2,000 excess showed very strong support for a flat-rate excess for building cover.

Regarding the dollar value of a flat-rate excess, submissions were more mixed, with a majority of submitters concerned that a \$2,000 excess would be unduly burdensome to EQC claimants.

Officials consider that a total GST inclusive excess of \$500 each for both building and land cover (i.e. a total of \$1,000 excess if there is both building and land damage) would strike a reasonable balance between efficiency, acceptability/affordability and recovery concerns.

¹⁸ According to the Reserve Bank of New Zealand online inflation calculator, CPI-indexing \$200 from quarter 1 1984 would result in an excess of \$678 in quarter 4 of 2020.

¹⁹ This is EQC's probable maximum loss event, the event that will inflict the largest modelled loss within a given timeframe. For EQC that is a large (magnitude 7.5) Wellington earthquake, which has an expected return period of about once every 840 years.

Claims excesses applicable to multi-unit buildings (MUBs)

The proposed claims excesses for MUBs retain the same structure as at present, updated to reflect the \$500 fixed claim excess, and discontinuation of the percentage-based excesses.

Therefore, the current maximum excess for land cover of \$5,000 per claim is retained. This means that any MUB containing 10 or more dwellings will pay an excess of \$5,000 on any land claim.

3.3A Which of these options is the proposed approach?

We recommend a flat rate, GST inclusive, per-dwelling excesses of \$500 each for building and land cover for all residential buildings and the retention of the current maximum excess for land cover of \$5,000 GST inclusive. We consider this proposal will support the clarity, certainty, and durability of the EQC Act. Moving from a percentage-based excess with a minimum and a maximum to a flat-rate excess, intermediate between the current minimum and maximum excesses, means that lower-value claims will pay higher excesses than at present and higher-value claims will generally pay lower excesses. With a flat rate of \$500 excess for a land claim and retention of the current \$5,000 maximum excess for land claims, no land claimant would be worse off as \$500 is the current minimum excess for land claims.

Reducing the total excess amounts for most larger claims is considered reasonable, as the larger claimants are those who have suffered the greatest loss, and the change is likely to help expedite timely and effective recovery of quality housing. The increases proposed to the minimum building cover excess are less than the current minimum amounts adjusted for inflation since they were introduced.

Issue 4: Updating EQC’s ability to provide insurer discounts

3.4 What options have been considered?

Status quo

Section 23 of the EQC Act provides for the setting, by regulation, of insurance premiums (levies) payable to EQC by a private insurer when the insurer issues a relevant insurance contract. The premium amount becomes a debt due by the insured person to the insurer and may be recovered by the insurer. As a carry-over from the Earthquake and War Damage Act 1944, section 23(4)(a) also provides, subject to any regulations made under the Act, that EQC may, “as it thinks fit”, discount the premiums payable to EQC by private insurers.

Since 1944, EQC has used its discounting discretion to allow private insurers to retain [25] of the premiums payable to EQC.

Problem definition

It is not clear in the EQC Act when and to what extent discounts should be used. The provision for EQC premium discounts is out-of-line with standard policy and legislative practice as Crown compensation for costs incurred in collecting a tax or a levy are rare in law.

The current provision and historic, percentage-based discounting practice may result in insurers receiving a discount for more than the actual and reasonable costs they incur. Also, the large increases in EQC premiums over recent years (without a consequent change to the discount rate) have resulted in insurers retaining considerably larger amounts of EQC premiums than in the past.

Decision-making criteria

The key criteria applied to the option analysis were:

- alignment with standard policy and legislative practice around collection of Crown levies
- the extent a legislative provision is necessary to enable cooperation between EQC and private insurers around premium payments/recovery or other costs incurred by private insurers in supporting effective implementation of the EQC scheme
- the extent that possible private insurer responses to any change might:
 - disrupt recently negotiated arrangements between EQC and private insurers such as the Insurer Response Model (IRM) and associated Data Sharing Agreement
 - impact on the premiums paid by residential property owners for their private and EQC insurance cover.

Options considered

- **Status quo:** No change to the current legislative approach to insurer premium discounts.

- **Option 1:** Remove the discounting provisions from the EQC Act so that any future cooperation between EQC and private insurers around premium payments/recovery and any other EQC scheme costs would be achieved by other methods such as negotiated commercial arrangements.
- **Option 2:** Retain a provision for insurer premium discounts but amend the EQC Act to clarify the purpose of the discount as a discretionary statutory transfer payment (not a negotiated or precisely calculated compensatory payment) and to set clear parameters around the exercise of EQC's discount discretion.

Options analysis

Although maintaining the status quo would be the least disruptive option, it is not recommended as:

- Enabling discounts or retainers for private persons required by law to collect a government tax or levy are very unusual (but not unique). More general examples of the usual practice that the private collector not retain a share of a tax or levy, include PAYE income tax, GST and ACC levies.
- More specifically general insurers also pay the Fire and Emergency levies (FEL) on a wide range of general insurance policies, including residential insurance policies. This long-running practice stems from the insurer-owned origins of fire brigades. The Fire and Emergency New Zealand (FENZ) Act 2017 (and antecedent legislation) does not provide for insurer discounts on FEL. While FENZ benefits insurers by reducing their liabilities (for example, reducing fire damage claims), EQC also substantially reduces private insurer liabilities, by taking on large natural disaster exposures that might otherwise fall on private insurers.
- The current arrangements are not necessary to enable cooperation between EQC and private insurers around premium payments/recovery or any other EQC scheme costs.

With respect to the other options:

- **Option 1:** Removing the discounting provisions from the EQC Act would align the Act with standard policy and legislative practice around collection of Crown levies (i.e., no statutory compensation for levy collection costs). Consultation with ICNZ indicated that there would be strong insurer objections to removal and some likely demands to renegotiate the IRM.
- Private insurers say there are significant operational costs in collecting EQC premiums from their customers and otherwise managing EQC-related transactions. The insurers consider that the discounting option helps to offset those costs and stated that removal would disrupt long-standing arrangements that have worked well. They expect that removal would create new costs that would likely be passed on to their customers in the form of premium increases.
- On balance, we do not consider these insurer objections outweigh the reasons for removal. The issues insurers raise are inconsistent with standard legislative practice and any impacts of a change are likely to be transitional and, where appropriate, manageable through negotiated commercial arrangements. In consultations EQC supported removing the discount, in part as it would clarify that any remuneration arrangements between EQC and insurers are expected to be based on entirely commercial grounds, rather than the current blended approach (of the discount plus other commercial arrangements). Future negotiations between EQC and insurers would provide an opportunity to address insurer concerns.

If EQC's premiums are set according to proposed pricing principles (T2020/2886 refers), then, in principle, the removal of the section 23 discount should not change the total amount paid by residential property owners for their EQC and private insurance cover. That is because, under the status quo, EQC would calculate its breakeven premium rate and then adjust it upwards to account for the ^[25] discount. If the discount is discontinued, the breakeven levy will be ^[25] lower, and private insurers can be expected to increase their private premiums, excluding the levy, to recover the lost revenues. The net effect on residential property owners and the insurers' revenue being zero.

- In practice, however, insurer price responses would depend on a range of market and internal considerations and vary between insurers. Possible insurer responses could include adding the full ^[25] revenue into their premiums, adding their actual costs to premiums, recovering the revenue from EQC in another way, or not increasing premiums at all. Therefore, the price impacts on individual policy holders, or classes of policy holders, cannot be predicted with certainty. However, any price effects appear likely to be modest. If private insurers fully recovered the lost discount revenue from policies with EQC cover attached, the price increase would be up to ^[25] per dwelling per annum ^[25]
- **Option 2:** Retaining provision for insurer premium discounts with clarifying amendments would be a substantial improvement over the status quo and would likely reduce the likelihood of private insurer objections. However, this option would maintain an unusual and unnecessary legislative approach, given that retaining a legislative provision for an insurer discount is inconsistent with standard policy and legislative practice around collection of Crown levies..

3.4A Which of these options is the proposed approach?

In the likely absence of any cost impact on residential property owners, we recommend Option 1, removal of the discounting provisions from the EQC Act to:

- better align the EQC Act with the standard government policy and legislative approach to setting and charging levies (i.e., private persons required to collect a government tax or levy are almost always not compensated by the government for doing so)
- enable premium payments/recovery and other EQC scheme cost issues to simply be addressed as part of the cooperation arrangements negotiated between EQC and private insurers.

The proposed change will, by aligning with standard legislative practice, support durability of the EQC Act.

Issue 5: Clarifying what the Natural Disaster Fund can be spent on

3.5 What options have been considered?

Status quo

The Earthquake Commission Act (EQC Act) currently authorises the Minister Responsible for EQC to set EQC premiums (referred to in this RIA as the 'levy'), which accumulate within the Natural Disaster Fund (NDF).

The EQC is funded almost exclusively by these levies. While the EQC has relatively limited discretion as to how it settles claims (a statutory entitlement), the Board has a significant amount of discretion as to how, or whether, it funds priorities relating to its education and research functions. While the Minister may direct the EQC, as a Crown agent, delegation to the Board has a number of benefits that include separation from operational detail, time consistency, and a close association between insurance and risk mitigation functions.

Legislation Design Advisory Committee (LDAC) guidelines specify that empowering provisions should state the basis for levies and that charges should bear a proper relationship to the cost of providing a service. However, in contrast to LDAC guidelines the basis for EQC levies is not included in the EQC Act.²⁰

The Cabinet paper '*Modernising the Earthquake Commission Act*' (April 2021) and supporting RIS '*Earthquake Commission Act 1993 modernisation*' (March 2021) sought agreement to changes to improve transparency around the purpose, and administration, of the EQC scheme. The papers sought agreement that levies should be set to cover the expected future costs of insurance and related costs.

While this clarifies that levies may only recover the expected costs of insurance, it does not specify what the levies can be used for.

Section 15 of the current EQC Act ("*Money payable out of the fund*") currently allows the EQC to pay any expense that it incurs in relation to its functions under the Act. The EQC's functions have been expanded to allow it to contribute to wider Government priorities in the disaster management and/or community resilience space. There is currently no requirement that the EQC apportion costs between insurance and non-insurance duties.

While in practice, public policies (e.g. the clean-up of silt for uninsured homeowners in Edgecumbe in 2017) has been publicly funded in the past, there is no statutory test to determine when funding should be provided. On a day-to-day operational basis, any statutory test / requirement for the apportionment of costs is likely to be most relevant to EQC in exercising its research and education functions, through which EQC:

- improves knowledge and professional practices in order to reduce the Government's liabilities from natural disasters and make communities more resilient to such events

²⁰

See chapter 17 of the Legislation Guidelines: 2018 edition: <http://www.ldac.org.nz/guidelines/legislation-guidelines-2018-edition/issues-particularly-relevant-to-empowering-secondary-legislation/chapter-17/>

- helps raise awareness of the ways individuals and communities can better protect their property. Stakeholders have expressed strong support for these educational activities.

Problem definition

EQC premiums are collected as a compulsory charge applied to residential insurance policies. The compulsory nature of the charge suggests that these premiums should be treated as a levy.

LDAC Guidelines provide guidance to ensure transparency around compulsory charges. These guidelines require that:

- legislation should lay out how levies are determined
- there should be a proper relation between the levy amount charged and the particular function concerned, and
- levies should only be imposed if it is appropriate for a certain group to contribute money for a particular purpose.

Feedback from LDAC has suggested that the EQC Act is not consistent with best practice as the levy-setting process needs to be transparent and there needs to be a clear basis for how the rate of levies is determined. Leaving the allocation of costs between premiums and public funding to a Board, as occurs in section 15 of the Act, is not best practice.

By way of contrast the Public Inquiry into the EQC indicated that EQC's research and education program is well respected in New Zealand and internationally and that research for infrequent events may not be otherwise funded. The Inquiry indicated that it was important that the EQC retain adequate funding and be given the ability to determine its own research priorities.²¹

While, in practice, the Board determines its research priorities, the Responsible Minister may direct Crown Agents via a direction made under section 103 of the Crown Entity Act and Section 12 of the EQC Act. The proposed criteria applying to the use of NDF funds would apply in the same way to both the Minister and the EQC Board. Education and research that cannot be funded via the NDF would require supplementary funding provided by the Crown.

Decision-making criteria

Recognising the perspectives provided by the Inquiry and the LDAC requires a balancing of objectives.

In assessing the options, we have considered:

- transparency – does the statutory framework provide and disclose a basis for decision-making
- flexibility – does the solution retain the strengths of the current system, that allows the EQC flexibility to determine its research priorities, which has led to research into low probability high impact events that would not be funded otherwise.

²¹ See pages 67-68 of the report of the Public Inquiry into EQC: <https://eqcinquiry.govt.nz/assets/Inquiry-Reports/Report-of-the-Public-Inquiry-into-EQC.pdf>

- durability – the system should provide a framework that is able to evolve in response to pressures arising from natural disasters, public concern, or perceived performance issues.
- accountability – the statutory test should provide a basis for accountability as to how public funds and/or levies have been spent.
- fairness – the scheme should produce outcomes that are seen to be fair for property owners.

Options considered

Our advice considered three options involving:

Option One – the status quo: the current section 15 could be retained granting the EQC full legal authority to charge any (insurance or non-insurance) cost associated with its functions to the NDF.

Option Two – limit the NDF to insurance claims costs: the Act could provide a hard statutory test to specify that the NDF can only be used to cover the direct costs of EQC insurance (i.e. claims, administration, and associated costs such as reinsurance).

Option three – amend the Act to specify that the NDF may be used to pay for direct insurance costs and any research or education that either provides a benefit to insured homeowners (i.e. levy holders) or reduces the costs of the scheme.

Options analysis

A summary of our options analysis has been included in Table 1 below.

Option One – the status quo:

Most insurers will invest to better understand the risks they cover or to encourage clients to reduce risk over time. While the Minister may direct the EQC's (as a Crown agent), the current delegation to the Board has a number of benefits that include separation from operational detail, time consistency, and a close association between insurance and risk mitigation functions.

The main benefits of the current section 15 is that it provides the EQC substantial flexibility to determine its education and research priorities. The Inquiry has indicated that the EQC's education and research programme is well regarded and has delivered significant value.

The main shortfalls relate to the lack of transparency and accountability issues highlighted by the LDAC. Without statutory guidance uncertainty exists as to how future Commissioners may prioritise research and educational expenditures.

Without statutory guidance the quality or composition of future research grants could change. Perceived fairness issues that arise as only property owners cover the cost could lead to pressures to amend the Act (a durability issue).

Option two -- limit the NDF to insurance claims costs: the strengths of option two are the inverse of the status quo. Hard criteria are easy to assess, which provides a strong basis for transparency and accountability.

The key weakness of this proposal is that it would significantly constrain the EQC by preventing it from innovating or spending money in even clear-cut cases where an education or research initiative could save significant future insurance costs. Criticism that EQC could have mitigated loss may generate pressure to change the Act after a large event (another durability issue).

In considering this option, we note the Inquiry supported EQC retaining flexibility to allow the EQC to determine its research and education priorities. This option would preclude this happening unless the EQC received public funding.

The benefit of public funding is that it would recognise the public good created by pure scientific research or uncertain payoff from education. But given the severity of the risks that low probability natural disasters represent to New Zealand, we would recommend that any funding be provided as a fixed (i.e. permanent) baseline. While the Government funds several annual contestable research grants, there is a risk that annual research grants to avoid insurance losses arising from very low probability events may be crowded out by other research priorities (e.g. innovation, sustainability, or economic growth).

Option three – limit the NDF to be used to pay for direct insurance costs and any research or education that either provides an expected benefit to insured homeowners (i.e. levy holders) or reduces the costs of the scheme:

Option three represents a mix of the strengths associated with options one and two.

In practice, the benefit associated with education and/or research is highly uncertain, suggesting that it would be difficult to define a tightly worded statutory test. While some investments in research and education may produce an immediate benefit for insured homeowners or the insurance scheme, investments in pure scientific research may act more like a public good providing general (non-excludable) benefits over a longer time period.

As such, an expected benefit test will always be subjective and may act more as a process check. The EQC would still have a lot of discretion, but would face a new legal test requiring it to show that it has considered (and documented) whether the expenditure benefits were considered within a sufficiently robust process. The benefit could be to either the insured property owners or the scheme as a whole. We consider this approach balances the abovementioned benefits of the current delegation to the Board of decision-making on spending, against the need for adequate transparency and accountability mechanisms around EQC's research spending.

The transparency and accountability associated with this test are considered an improvement over the status quo, without placing inflexible limitations on EQC spending. In practice, any perceived issues relating to transparency may be addressed via strong non-statutory disclosures released on the EQC website.

This principle-based test may not be durable if it is badly applied. For this reason, we have recommended that the Act also include an option for public funding of EQC's contribution to broader public policy process (beyond its insurance focus, such as in the community resilience space) to allow the Crown's funding strategy to adapt over time. We anticipate that criticism of EQC spending could trigger provision of additional public funding without a need to further amend the Act.

Table 1: Analysis of options for Natural Disaster Fund apportionment

	Transparency around how levies are set	Flexibility to allow the EQC to determine its research priorities	Durability - the framework can evolve as appropriate	Accountability - the EQC's funding should be disclosed and subject of review	Fairness to property owners	Overall assessment
Option one: Status quo	0 The Act does not meet this criterion as it does not specify how costs should be apportioned between property owners and the Crown.	0 The current Act easily meets this criterion as EQC has significant flexibility to determine its research priorities to better understand natural disaster risk.	0 The Act fails this test as the LDAC has submitted that the Act does not meet modern drafting standards and requires revision. - any future instances where EQC has incurred significant non-insurance costs may generate pressure for future statutory change.	0 The Act may meet this criterion. However, while the Act includes accountability mechanisms, effective review is complicated by the lack of clear criteria.	0 The current Act does not discourage or encourage fair outcomes. While the EQC has always sought to safeguard fairness, the Act technically authorises costs that may seem to be unfair to be allocated to only insured homeowners.	0
Option two: Insurance Costs only	++ A restrictive test would be transparent for property owners.	-- The restrictive nature of this option would exclude the EQC from funding research or education that reduces future cost.	- evidence that the EQC has missed obvious options to reduce cost may trigger a need for statutory change.	++ a hard criteria-based test limiting payments to direct insurance costs is easy to assess so offers the most accountability.	+ a hard criteria-based test may be perceived as fair as it prevents research that provides wider benefits from being charged only to homeowners.	+++
Option three: insurance, research, and education	+ A principles-based test is more transparent than the status quo, while having benefits in terms of flexibility.	++ a principles-based test requiring the EQC to consider whether a benefit exists would allow EQC to fund beneficial research and education. The test creates an expectation that work that does create a significant benefit should be funded.	++ the flexibility in this test could prove durable if it was combined with an option for public funding to allow the Crown's funding strategy to evolve in response to disasters, a change in the nature of overall cost of research, or public concern.	+ a principles-based test requiring the EQC to consider whether a benefit exists is a process-based test. The benefits may be difficult to prove in practice, but Ministers of Finance and the Finance and Expenditure Committee can test EQC process or how the EQC has assessed the benefits.	+ while pure science research is a public good, the EQC must determine that the research offers a benefit to insured property owners or the scheme as a whole.	++++++

3.5A Which of these options is the proposed approach?

New Zealand's geography and our exposure to natural disasters informs how we have weighted the decision-making criteria. The infrequent nature and severity of natural disasters supports provision of a degree of independence to ensure research investment occurs and that steps are taken to ensure that the public understand natural hazard risks and what they can do to build their resilience.

While hard prescriptive spending limits offer clear benefits over the status quo in terms of transparency and accountability, constraints of this sort may undermine the benefits of the current EQC scheme. While constraints provide certainty that levies are fair for insured property owners, current research expenditures remain moderate (around \$17 million). With hard limits there is a risk that the EQC scheme could become very reactive (i.e. the scheme would place insufficient weight on investing to avoid future costs/loss).

For this reason, we have recommended a flexible solution based on option three, which requires that the EQC consider whether spending provides a benefit for either insured property owners (who pay the levy) or the future costs of the scheme as a whole.

An expected benefit test for education or research involves a significant amount of subjectivity, so the test could theoretically justify a range of different expenditures or may suffer from a lack of transparency and/or accountability. These potential shortfalls can be addressed by the EQC through good administrative processes that involve documented consideration of the benefit, public consultation, and public disclosures by the EQC.

Public funding provided in the form of an annual baseline provides an alternative that the Government could consider. As the review of the EQC Act has focussed on developing a permissive principle-based legislative framework, we do not propose to lock this requirement into legislation.

The proposed solution would provide future Governments options as to how the EQC is funded by:

- providing the EQC with a new statutory test requiring it to consider the benefit of its spending to determine whether it benefits either insured property owners or the insurance scheme
- including a new statutory power allowing the EQC to enter into a services agreement, which the Government could use to provide public funding (if required). We note this is proposed in an earlier Cabinet paper 'Modernising the Earthquake Commission Act' (April 2021) and supporting RIS 'Earthquake Commission Act 1993 modernisation' (March 2021).

The EQC's annual priority setting process (i.e. consultation with the Minister on the Statement of Intent) may provide an opportunity to discuss the benefits of the EQC research and education to determine whether public funding is required.

We think that a flexible statutory framework will prove the most durable over time. Public concerns, an increase in the overall cost for property owners, or a move to increase the share of funding for pure scientific research increases may prompt a discussion on whether the Crown should contribute to the costs of research.

Section 4: Impact Analysis (Summary topics)

4.1 Summary table of costs and benefits

Affected parties (identify)	Comment: nature of cost or benefit (eg, ongoing, one-off), evidence and assumption (eg, compliance rates), risks	Impact <i>\$m present value where appropriate, for monetised impacts; high, medium or low for non-monetised impacts</i>
Additional costs of proposed approach, compared to taking no action		
EQC	<p>The proposals are expected to have no, or minor, cost implications.</p> <p>The proposed limit to Natural Disaster Fund expenditure (issue 5), in order to focus on direct insurance costs and any research or education that either provides an expected benefit to insured homeowners (i.e. levy holders) or reduces the costs of the scheme, will require EQC to demonstrate that expenditure meets this gross benefit test. This is likely to cause some administrative and resourcing cost compared to the status quo.</p>	Low.
	EQC estimates the proposed changes to cover for land structures (issue 2) would increase the cost of EQC settlements for claims involving retaining walls by about 40 percent. The expected impact on annual costs is difficult to quantify due to data limitations. EQC estimate an upper bound of about \$8.7 million per annum, in normal years without large claims events (based on data from 2014-2020).	Medium
	If any or all of these proposals are implemented, the expected cost impacts will be reflected in future advice regarding the appropriate levels of EQC premium.	Low
Private insurers	Revenue lost due to no longer receiving a discount from EQC from the levies insurers collect on EQC's behalf (issue 4). [25]	[25]
Insured homeowners	The proposed changes to excesses (issue 3) will mean most owners of standalone dwellings or smaller MUBs will pay more for lower-value claims compared with the	Low-Medium.

	<p>status quo. The current minimum building excess is \$200 multiplied by the number of dwellings in the building (e.g. in the case of an apartment building), or 1% of the settlement amount, whichever is greater. The proposal is to amend building excesses to a flat rate of \$500 per dwelling. EQC estimates that approximately 86% of homeowners will pay a higher excess on EQC building cover (up to \$300 more per building claim for a single dwelling). No land claimants would be worse off as \$500 is also the current minimum for land claims.</p> <p>The proposed changes to EQC cover for land structures (issue 2) will result in reductions in settlements to claimants in rare circumstances (i.e. where both the repair cost, and the indemnity value plus the value of the damaged land, exceed the value of the proposed monetary cap).</p>	
Total Monetised Cost	Not available	Not available
Non-monetised costs		Low

Expected benefits of proposed approach, compared to taking no action

EQC	<p>Clarifying what Natural Disaster Funds are spent on (issue 5), and updating EQC's ability to provide insurer discounts (issue 4), will make for a more equitable scheme, ensuring EQC levies are used for appropriate purposes. Introducing measures to address these issues will support a more modern EQC Act which is in line with legislative best practice and encourage greater public understanding of and confidence in the EQC scheme. This should support EQC's reputation and interactions with the public.</p> <p>Higher insurance excesses for low value building claims (issue 3) is expected to lead to a \$1.2 million reduction in EQC's average annual claims costs. For building claims in the case of a reference event (large Wellington earthquake) the new flat-rate excess is expected to result in a claim number reduction of 2.8% and a reduction in EQC claims liability of \$5 million.</p> <p>Known excess amounts prior to settlement will also help to discourage claims worth</p>	<p><i>Natural Disaster Fund changes</i></p> <p>Low</p> <p><i>Changes to EQC excesses</i></p> <p>\$1.2 million reduction in EQC's average annual claims costs.</p> <p>In the case of a reference event, a reduction in EQC claims liability of \$5 million.</p> <p>Note that these numbers relate to only building claims as, due to data limitations, EQC is unable to estimate the costs of changes to land excesses. We expect the impacts of</p>
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	less than \$500, which supports administrative efficiency for EQC (including by freeing up limited claims handling capacity for high-value claims). A simpler process for calculating excesses will provide further efficiency gains.	these changes to be Low.
Private insurers	<p>The proposed changes to EQC cover for land structures (issue 2) are expected to reduce claims lodged with private insurers for these structures. Officials have not attempted to quantify the reduction. It is expected to be a small fraction of the additional costs to EQC (i.e. the primary and intended beneficiaries of the additional EQC costs is EQC claimants)</p> <p>Improved clarity and certainty around EQC claims excesses (issue 3). Less complex excess calculations also support administrative efficiency.</p>	Low
Insured homeowners	<p>Updating excesses for building and land cover (issue 3), clarifying what NDF funds are spent on (issue 5), and updating EQC's ability to provide insurer discounts (issue 4), will make for a more equitable scheme, ensuring that the costs homeowners pay to access EQC cover are set at an appropriate level and used for appropriate purposes over time.</p> <p>Additionally, the introduction of flat rate rather than percentage-based excess (issue 3), and clear monetary caps for retaining walls (issue 2), means homeowners will be able to know more about their insurance entitlements and liabilities ahead of an event, and plan accordingly. EQC claims data suggests that the great majority of EQC claims settlements involving land structures would be either increased or unchanged by the proposals.</p> <p>High value claims for large multi-unit buildings will pay a lower excess (issue 3).</p> <p>The proposed changes to EQC cover for land structures (issue 2) will benefit the great majority of EQC claimants affected by the change.</p>	Low-Medium
Total Monetised Benefit	Not available	Not available
Non-monetised benefits		Low-Medium

4.2 What other impacts is this approach likely to have?

There has been significant previous public consultation on the issues with the current EQC Act and potential options for change in 2015 and during the more recent Public Inquiry, which included extensive consultation with the people of Canterbury. Consequently, the Minister Responsible for the EQC decided not to undertake a full public consultation process, including with iwi/hapū, or to consult on an exposure draft of the proposed EQC Bill. The Treasury has instead undertaken a targeted consultation process with key stakeholders on relevant proposals.

The package of proposals to modernise the Act do not propose fundamental reforms and are fairly complex and technical in nature. The targeted consultation process does create a risk that groups not included in the targeted consultation could raise technical or other issues at Select Committee that officials have not considered. However, we do not think this presents a significant risk to any particular issue covered in this RIS. While the public is likely to have an interest in increased excesses (issue 3) the proposed excess amount is consistent with conclusions reached after considering 2015 public consultation feedback on this issue.

Lack of consultation with iwi/hapū also creates specific risks for the legislative process. Officials could not identify any issues regarding the EQC scheme that iwi might have a particular or distinctive interest in, and expect to be consulted on. EQC cover attaches to all residential buildings with a fire insurance policy, which includes iwi-based living and ownership arrangements such as papakāinga. As with other groups not included in the targeted consultation process, there is a risk that iwi-specific issues associated with the EQC scheme may be raised at Select Committee.

We note that we did not consult Te Puni Kōkiri on the EQC Act policy process.

Section 5: Stakeholder views

5.1 What do stakeholders think about the problem and the proposed solution?

Consultation as part of the current EQC Act review

The Treasury has worked collaboratively with EQC throughout the current EQC Act review process. Treasury has also consulted with a targeted group of stakeholders, relevant government agencies, and other public bodies during 2020 and 2021 to inform policy development:

1 relevant government departments or other public bodies:

- 1.1 EQC and the Reserve Bank of New Zealand have been consulted on all issues. The Department of Prime Minister and Cabinet (Policy Advisory Group) has also been informed on all issues.
- 1.2 The Ministry of Business, Innovation and Employment was consulted on all issues except issue 1, a time bar on EQC insurance claims, and issue 5, clarifying what the Natural Disaster Fund can be spent on.
- 1.3 The Ministry of Justice was consulted on the proposed time bar on reopening claims (Issue 1).
- 1.4 The Department of Internal Affairs and Land Information New Zealand were consulted on issue 2, monetary caps on retaining walls, bridges and culverts; issue 3, excesses; issue 4, updating EQC's ability to provide discounts; and issue 5, clarifying what the Natural Disaster Fund can be spent on.
- 1.5 The Ministry for the Environment was consulted on issues 2 (monetary caps on retaining walls, bridges and culverts) and 5 (clarifying what the Natural Disaster Fund can be spent on).
- 1.6 The Public Service Commission (PSC), and Office of the Auditor General (OAG) were consulted on issue 5, clarifying what the Natural Disaster Fund can be spent on.

2 relevant private sector organisations and public consultation processes:

- 2.1 The Insurance Council of New Zealand (ICNZ) has been consulted on all the policy issues contained in this RIS except issue 5 (regarding clarifying what the Natural Disaster Fund can be spent on).
- 2.2 The former EQC Claimant Reference Group was consulted at an early stage on reopened claims which relates to issue 1, a time bar on reopening EQC claims.
- 2.3 Early thinking on the issues surrounding reopened EQC claims (which has informed work on issue 1, a time bar) and monetary caps on retaining walls, bridges, and culverts (issue 2) was shared with the New Zealand Bankers' Association who consulted their members. We received feedback from BNZ on the issues which was considered in policy development.

ICNZ has raised concerns about tight consultation timeframes

ICNZ has raised concerns that consultation timeframes have been too short for adequate consideration of complex issues and that they have been consulted only on specific policy issues rather than being given an opportunity to comment on the EQC Act modernisation policy package as a whole. To ensure that the Select Committee has sufficient time to fully consider any concerns raised by stakeholders in submissions, including by ICNZ, the Minister intends that, following the first reading of the bill, the

Select Committee be provided the usual six months to report back to House.

Stakeholder perspectives

The Treasury has undertaken a targeted consultation process with ICNZ on all topics covered in this RIS except issue 5, clarifying what the Natural Disaster Fund can be spent on.

The targeted consultation process does create a risk that groups not included in the targeted consultation could raise technical or other issues at Select Committee that officials have not considered. However, we do not consider this to be a significant risk for any of the specific issues contained in this RIS due to their relatively minor and technical nature. Stakeholder feedback is broadly summarised as follows:

- **Issue 2 – Monetary caps on retaining walls, bridges, and culverts:** EQC support the proposed changes. ICNZ feedback on this issue included:

“We agree to separate monetary caps being introduced for retaining walls, bridges and culverts in principle, in the interest of certainty, fairness and the sustainability of the regime.

Our preference would not be to structure retaining wall cover on a per dwelling or residential basis for simplicity and as there is no clear connection between the number of dwellings/residential buildings and number of retaining walls a customer may have.”

- **Issue 3 – Updating excesses:** The proposed excess amount is consistent with conclusions reached after considering 2015 consultation feedback on this issue. ICNZ was informed that work on EQC excesses was being undertaken, but was not formally consulted on this issue as informal discussions with ICNZ indicated that the setting of altered EQC excesses are unlikely to significantly impact insurers’ interests. EQC confirmed a preference for Option 2
- **Issue 4 – Clarifying EQC’s ability to provide discounts:** ICNZ disagreed with the proposal to remove EQC’s ability to provide discounts to insurers from the legislation. Removing the discounting provisions from the EQC Act would align the EQC Act with standard policy and legislative practice around collection of levies, that is, no statutory compensation for levy collection costs. Consultation with ICNZ indicated that there would be strong insurer objections to the removal of the discount and likely demands to renegotiate EQC’s Insurer Response Model.
- **Issue 5 – Clarifying what the Natural Disaster Fund can be spent on:** Stakeholders outside the Crown were not consulted on this proposal. This is because EQC is already fully funded through levies, and the purpose of the proposal is to provide clarity that the EQC’s current insurance-related functions will continue to be funded in this way. Other proposals (covered in a separate RIS titled ‘*Modernising the EQC Act*’) have sought to expand EQC’s functions to contribute to wider government priorities. The proposal ensures any work Government directs EQC to do beyond its insurance-related functions would be funded by appropriation. Therefore, this proposal is more of a clarification of the bounds of the EQC’s mandate to spend the Natural Disaster Fund rather than creating any additional costs.

Relevant consultation during a previous review of the EQC Act

As part of a previous review of the EQC Act, a public discussion document was released in 2015 seeking feedback on reform proposals.²² In total, 63 submissions were received

from individuals and a range of organisations.²³ The Bill will draw heavily on information and feedback gathered during consultation processes associated with that review.

Relevant consultation during the Inquiry

Public engagement was a significant part of the Inquiry process.²⁴ We have drawn heavily on the content of the Inquiry report to inform policy development for the proposals.

22 *New Zealand's future natural disaster insurance scheme: Proposed changes to the Earthquake Commission Act 1993* (July 2015): <https://www.treasury.govt.nz/sites/default/files/2012-09/eqc-rev-discussion-doc.pdf>

23 Submissions in response to the 2015 discussion document are available on the Treasury website: <https://www.treasury.govt.nz/news-and-events/reviews-consultation/earthquake-commission-act-1993/earthquake-commission-act-submissions-received>

24 The Inquiry took an inquisitorial approach and documented the feedback gathered through the engagement process in a compendium to the Public Inquiry report, titled: *What we heard: Summary of feedback from the Inquiry's public engagement.*

Part 3: Implementation, monitoring, and evaluation

Section 6: Implementation and operation

6.1 How will the new arrangements be given effect?

The proposals will require legislative amendments to the EQC Act. The Treasury will work with EQC to develop any necessary guidance and communications to support implementation.

Once implemented, EQC will be responsible for ongoing public education regarding the EQC Act. The Treasury will remain the administering department for the revised EQC Act.

Should Cabinet agree to the amendments, a bill will be introduced to the House in 2021, with enactment expected to occur in late 2022.

As part of consultation on the EQC Act, ICNZ has requested at least 18 months between passage of the Bill and changes to the EQC scheme taking effect. Current timeframes for the Bill provide for this transitional period. Commencement dates will also be aligned with renewal of EQC reinsurance contracts, which will need to be renegotiated in line with the new EQC Act. Any new rules will apply to properties on an individual basis as individual insurance policies are renewed or new contracts are entered into, so that private insurers have the opportunity to price premiums based on the changes.

Section 7: Monitoring, evaluation and review

7.1 How will the impact of the new arrangements be monitored?

The role of the Treasury as the monitoring agency for EQC, is to assist the responsible Minister to carry out his or her role and to perform or exercise any or all of the following functions, duties, or powers:

- administering appropriations
- administering legislation
- tendering advice to Ministers, and
- any other functions, duties, or powers in the Crown Entities Act or another Act that may, or must, be performed or exercised by the monitoring agency.

The Treasury acts on behalf of the Minister and provides advice on setting expectations for EQC, and the performance of the Board and organisation overall. The Treasury also manages the process to appoint directors on behalf of Ministers and provides advice on the skills required for the Board. These business-as-usual monitoring mechanisms will enable the Treasury to evaluate the performance of EQC in implementing the new EQC Act over time.

We note that there are limitations in evaluating whether the impacts of the proposed changes materialise, given the nature of the proposals. This is because it is difficult to benchmark the status quo in order to evaluate the changes. However, we expect that trends in EQC’s general approach to its work will become evident over time. For example, given the modernising scope of the work, many of the proposals are intended to provide legislative clarity, such as clarifying EQC’s functions and objectives.

7.2 When and how will the new arrangements be reviewed?

There are no specific reviews planned for the proposals outlined in this RIS, beyond business-as-usual monitoring, policy review processes, and the five-yearly reviews of financial settings that are proposed elsewhere. This is largely due to the nature of the proposals being to *modernise* rather than fundamentally alter the scope and workings of the EQC Act.

The Treasury's business-as-usual commitment to an ongoing regulatory stewardship programme will ensure the EQC system is reviewed at appropriate intervals to determine whether it is still fit-for-purpose and likely to remain so. The first regulatory stewardship assessment of the EQC Act is expected to be published by the end of 2021, but will focus on the current EQC Act, rather than the proposed amendments.

Appendix: Topics excluded from this Impact Statement

The following topics were exempted from inclusion in this Impact Statement due to having no or only minor impacts on businesses, individuals, or not-for-profit entities:

- clarifying EQC's ability to delegate its settlement function to private insurers
- [33]
- updating the EQC Act exclusions in Schedule 2
- clarification of EQC's information sharing powers, and
- modernising the structure, management of and reporting required for the Natural Disaster Fund.