

The Treasury

Treasury Advice Related to Modernising the EQC Act Information Release

December 2021

This document has been proactively released by the Treasury on the Treasury website at:

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

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

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [25] appearing where information has been withheld in a release document refers to section 9(2)(b)(ii).

Copyright and Licensing

Cabinet material and advice to Ministers from the Treasury and other public service departments are © **Crown copyright** but are licensed for re-use under **Creative Commons Attribution 4.0 International (CC BY 4.0)** [<https://creativecommons.org/licenses/by/4.0/>].

For material created by other parties, copyright is held by them and they must be consulted on the licensing terms that they apply to their material.

Accessibility

The Treasury can provide an alternate HTML version of this material if requested. Please cite this document's title or PDF file name when you email a request to information@treasury.govt.nz.

Treasury Report: Coverage of Multi-Unit Buildings under the Earthquake Commission Act

Date:	10 October 2019	Report No:	T2019/3015
		File Number:	TY-2-1-17-2

Action sought

	Action sought	Deadline
Hon Grant Robertson Minister of Finance Minister Responsible for the Earthquake Commission	Note that changes to the definition of residential buildings to better recognise public areas used for residential purposes within Multi-Unit Buildings will be considered as part of the review of the Earthquake Commission Act.	Meeting with officials on Wednesday 23 October at 3.30 pm.

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Shivani Middlemiss	Analyst, Earthquake Commission Policy Team ^[39]	N/A (mob)	✓
Helen McDonald	Manager, Earthquake Commission Policy Team	^[35]	

Minister's Office actions (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: No

Treasury Report: Coverage of Multi-Unit Buildings under the Earthquake Commission Act

Purpose of report

1. In discussions with officials you indicated an interest in the coverage of Multi-Unit Buildings (MUBs) under the Earthquake Commission (EQC) scheme. This report outlines how the EQC scheme covers MUBs through the definition of residential buildings within the EQC Act.

Background

2. As part of on-going work, we have provided you with advice on the extent and cause of changes in property insurance markets. We have now obtained more comprehensive information on pricing and availability, and explored options for addressing any identified problems (T2019/2933 refers).
3. Early evidence indicates that insurance premiums have increased in high-seismic risk regions such as Wellington, moderately on average, but potentially more significantly for certain types of MUBs and a small proportion of high-risk/high-value houses. We are currently collecting further evidence on the number of MUBs affected by changes in property insurance markets.

MUBs under the EQC scheme

4. EQC provides natural disaster insurance for residential buildings and associated land. One of the underlying intentions for the EQC scheme is to protect homes. The EQC Act therefore provides a prescriptive definition of both a home – a dwelling, and what makes up a building with dwelling(s) – a residential building.

Defining residential buildings

5. In broad terms, a dwelling is a self-contained premises that is a home or holiday home for one or more people (see Annex 1 for the full definition of residential buildings and dwellings within the EQC Act).
6. The EQC Act defines the first component of a residential building as, “any building, or part of a building, or other structure (whether or not fixed to land or to another building, part, or structure) in New Zealand which comprises or includes 1 or more dwellings, if the area of the dwelling or dwellings constitutes 50% or more of the total area of the building, part, or structure.” Other components (including appurtenant structures and services) are included in the balance of the definition.
7. A building is classified as a residential building when 50% or more of its floor area is made up of dwellings (50% residential building test). Under the EQC Act, these properties receive cover for the entire building and corresponding insured land.
8. Conversely, properties are classified non-residential, when less than 50% of the total area is used for dwellings. These properties do not receive EQC cover for the entire building and may have less (or no) insured land. The areas covered by EQC for non-residential buildings with dwellings are limited to: the dwellings themselves; structures appurtenant to the dwellings (both within and external to the building); and associated

services. The area within a non-residential building not covered by EQC is subject to private insurance. This may increase the overall cost of a single insurance contract for the entire building and may lead to higher excesses.

9. MUBs can include any of the following:
 - a. a flat, terraced house or apartment on a cross-lease title connected to another flat (usually owned and insured separately),
 - b. a unit-title apartment, townhouse or flat owned and managed in accordance with the Unit Titles Act by a body corporate,
 - c. a building with more than one insured dwelling, for example a rural complex with more than one dwelling or a home with a “granny flat” attached,
 - d. a mixed-use building, such as an apartment or flat above a shop or other commercial premises,
 - e. part of a rest home or retirement village, and
 - f. forms of ownership such as company shares, freehold dwellings sharing a party wall, and some leasehold properties with attached dwellings.¹
10. The properties affected by the 50% residential building test are mostly MUBs, in particular mixed-use buildings, where parts of a building are used for commercial purposes.

Recognising areas outside of dwellings

11. Under the current definition of residential buildings, common areas are excluded from contributing to the 50% residential building test. Part of the policy rationale for this is to assign “ownership” of common areas between commercial and residential owners. For other dwellings, such as a house, entranceways and stairwells are included within the EQC cover, as they are within the area that comprises the dwelling.
12. The definition of residential buildings in the EQC Act could be amended to better include common areas used for residential purposes, particularly as the current definition remains unchanged since 1993.
13. The practical effect would be that common areas used by the residents, e.g. access corridors, lobbies, and residents’ car parking, would contribute floor area to the 50% residential building test for determining if a property is a residential building.
14. The beneficiaries of this change would be limited to owners whose buildings are non-residential under the current definition (i.e. buildings with less than 50% total area with dwellings) and become residential under the Act. The primary benefits would likely be:
 - a lower claims excess,
 - EQC repairing damage in common areas of the building, and
 - EQC covering more of the associated land.

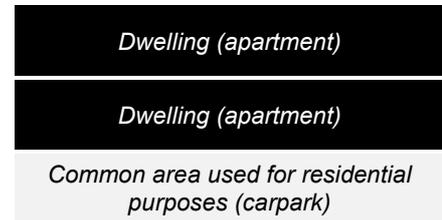
¹ <https://www.eqc.govt.nz/canterbury-earthquakes/progress-updates/complex-claims/multi-unit-buildings>

Stylised examples of MUBS

15. Below are some simplified examples of MUBs that would (not) be deemed a residential building under the current definition of the EQC Act. These examples assume that the building would be covered under a single insurance contract.

Example 1: stylised cross-section of a MUB with apartments

16. The whole building **would be** deemed a residential building, as dwellings contribute to more than 50% of the floor area. The common areas used for residential purposes do not contribute to the threshold, but would be covered by EQC.



Example 2: stylised cross-section of a MUB with dwellings and retail space

17. The whole building **would be** deemed a residential building, as the area used by dwellings is greater than 50%. Similar to the example above common areas used for residential purposes would not contribute to the 50% residential building test, but would be covered by EQC, as would the commercial space.



Example 3: stylised cross-section of a MUB with dwellings, offices and retail

18. The whole building **would not** be deemed a residential building, as the area used by dwellings is less than 50% of the total area. The dwellings and appurtenant residential carparks would be covered by EQC, but the commercial spaces would not. The entire building would be covered under a private insurance contract.



Changes in property insurance markets

19. Changes in property insurance markets are affecting MUBs (apartment buildings) with residents facing increasing premiums due to more granular risk-based pricing. In order for property owners to shift potential liability to the Crown, the 50% residential building test could be extended to include common areas used by residents.
20. By including common residential areas within the 50% residential building test for being a residential building according to the definition of the Act, EQC would cover a greater proportion of the seismic risk for MUBs. However, the change is unlikely to significantly increase the overall access and affordability of insurance due to the limited number of buildings that would be affected by the change.
21. A change in the definition of residential building may not necessarily result in a decrease in premiums for customers, as the private insurer response will also be shaped by market conditions. Also, insurer responses will only reflect risk transferred from insurers to EQC. Risks transferred from apartment building owners to EQC (most

notably via the reduction in claims deductibles) will not affect insurers' views of the building's risk and hence pricing.

22. A change in the definition may help customers following a natural disaster, as the excess on EQC would likely be lower than the excess on the commercial property insurance. A submission by the Marion Square Body Corporate to the Select Committee on the 2019 amendments to the EQC Act noted that the excess for natural disaster damage had increased substantially, regardless of the status of the building e.g. including for buildings that are over 100% of the New Building Standards (NBS) for earthquake rating.² Officials' advice on the EQC Amendment Bill was that the definition of residential buildings be addressed in a future Bill to draw on the lessons learnt from the Public Inquiry into the EQC.
23. A potential unintended consequence of changing the definition may be the strengthening of existing incentives to convert commercial office buildings facing higher private insurer premiums to MUBs, in order to access cheaper EQC cover. This would be a consideration if the definition is changed.

Next steps: review of the EQC Act

24. In order to change the definition, the EQC Act would need to be amended. The change in definition could be made in a more targeted amendment of the EQC Act, or within the current review of the EQC Act. Due to the timing of a more targeted amendment Bill, it is unlikely that the definition would be amended before the broader review of the EQC Act is scheduled to be completed in 2021-22. We therefore propose to consider the definition of residential buildings as part of the review of the EQC Act.

Risks

25. The Public Inquiry into the EQC will be reporting on operational experiences at the EQC after the Canterbury earthquakes. There are a wide range of issues that can most usefully be progressed after the Inquiry reports. We suggest that technical changes to the EQC Act be made after the Inquiry has reported in March 2020.

² https://www.parliament.nz/resource/en-NZ/52SCFE_EVI_77657_1874/9958e627f585dc071640c96d8c2c682412d573cf
T2019/3015Treasury Report: Coverage of Multi-Unit Buildings under the Earthquake Commission Act

Recommended Action

We recommend that you:

note that changes to the definition of residential buildings to better recognise public areas used for residential purposes within Multi-Unit Buildings will be considered as part of the review of the Earthquake Commission Act.

Helen McDonald
Manager, Earthquake Commission Policy Team

Hon Grant Robertson
Minister of Finance
Minister Responsible for the Earthquake Commission

Annex 1: Definitions of dwelling and residential building under the EQC Act

26. The definition of dwelling is as follows:

Dwelling means, subject to any regulations made under this Act, any self-contained premises which are the home or holiday home, or are capable of being and are intended by the owner of the premises to be the home or holiday home, of 1 or more persons.

27. The definition of residential building is as follows:

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

(b) any building or part of a building (whether or not fixed to land, or to another building, part, or structure) in New Zealand which provides long-term accommodation for the elderly, if the area of the building which provides long-term accommodation for the elderly constitutes 50% or more of the total area of the building, part, or structure:

(c) every building or structure appurtenant to a dwelling referred to in paragraph (a), or a building or part of a building referred to in paragraph (b), and that is used for the purposes of the household of the occupier of the dwelling or for the purposes of the residents of the building or part:

(d) all water supply, drainage, sewerage, gas, electrical, and telephone services, and structures appurtenant thereto—

(i) serving a dwelling referred to in paragraph (a), or a building or part of a building referred to in paragraph (b), or surrounding land; and

(ii) situated within 60 metres, in a horizontal line, of the dwelling or building or part; and

(iii) owned by the owner of the dwelling or building or part, or by the owner of the land on which the dwelling or building or part is situated.