

The Treasury

Treasury Advice Related to Modernising the EQC Act Information Release

December 2021

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Treasury Report: Future EQC Policy Work: Scope and Timing for a Review of EQC Scheme and Act (Report 1 of 2)

Date:	12 March 2020	Report No:	T2020/212
		File Number:	TY-2-1-17-2

Action sought

	Action sought	Deadline
Hon Grant Robertson Minister Responsible for the Earthquake Commission	Discuss with officials timing, scope and links with other work of the review of the EQC scheme and Act.	Meeting is scheduled for 17 March 2020.

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Steve Cantwell	Principal Advisor, Earthquake Commission Policy Team ^[39]	[35]	N/A (mob) ✓
Helen McDonald	Manager, Earthquake Commission Policy Team		

Minister's Office actions (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: No

Future EQC Policy Work: Scope and Timing for a Review of EQC Scheme and Act (Report 1 of 2)

Purpose of Report

1. The purpose of this report is to provide information to support a discussion with you regarding the potential scope and timing of the future review of the Earthquake Commission Act (the EQC Act), including:
 - process and timing for that review, and its links to related shorter-term work
 - your level of ambition for a review of the EQC Act, and
 - our proposal regarding how the current policy rationale for the EQC scheme should be utilised in preparing advice on residential property insurance and the findings of the Public Inquiry into the Earthquake Commission, as outlined in the companion report T2019/4058 *Future EQC Policy Work: Policy Rationale and Intervention Model (Paper 2 of 2)*.
2. Please read this report before its companion report.

Background

3. A review of the EQC Act was first announced by the previous Government in 2012. That review envisaged a comprehensive policy and legislative review, culminating in a new EQC Act. Reform of the EQC Act, and associated policy issues, has been on Treasury's work programme since then. The EQC Amendment Act 2019 drew on that work to address several high-priority reforms. It increased EQC building cover from \$100,000 to \$150,000, exited EQC from contents cover, extended claims filing deadlines, and improved EQC's information-sharing powers.
4. During the policy process associated with the 2019 Amendment Bill, the previous Minister Responsible for EQC indicated to Cabinet that she envisaged that the EQC Act would be substantively reviewed following the Public Inquiry (CAB-18-SUB-0081 refers).
5. We would like to test if this is also your intention, ahead of the impending release of the findings of the Public Inquiry into EQC (the Inquiry). If so, some of the Inquiry's recommendations are likely to be best addressed as part of the wider review of the EQC Act.
6. Other current policy work that also touches on EQC policy or legislation includes a May 2020 report-back to Cabinet on monetary caps for EQC building cover (DEV-19-MIN-0332 refers) and a proposed 2020 bill to amend the EQC scheme's coverage of mixed-use buildings that contain one or more dwellings (T2020/132 refers).

Analysis

7. Once the Inquiry reports, you will face a key choice regarding the scope of the follow-up policy processes.

8. Broadly we see three options, in order of increasing ambition:
 - a **targeted reform** that identifies and implements a small set of discrete, high-priority changes, akin to the 2019 EQC Amendment Bill
 - an **evolutionary reform** that thoroughly reviews the EQC and the EQC scheme, while retaining core features of the current design (those features include that first-loss EQC cover is provided to homeowners by compulsory attachment to private insurers' fire cover; the community rating of EQC premium, and that EQC is able to, but not required to, handle its own claims), and
 - a **first-principles review** that retests the objectives motivating the EQC intervention in insurance markets, and evaluates the EQC scheme design, against other intervention models. If the EQC model is endorsed, this would then become an evolutionary reform. If another model is preferred this would then become a **comprehensive reform** initiative.
9. Both the current property markets work, and the Inquiry's findings, will likely help inform your judgement whether to proceed with an evolutionary or first-principles reform. The current property insurance markets work will require some first-principles analysis to evaluate the options (options include across-the-board or targeted increases in EQC monetary caps on cover, or targeted natural hazard reinsurance) as these options could be consistent with different purposes for the EQC scheme and a change in role for the EQC.
10. The Inquiry's findings are likely to, at least implicitly, suggest whether the current EQC scheme design is fit for purpose. The extent to which the decisions from these areas of work are consistent with the current purpose of the EQC scheme will be a key determinant of whether the review should adopt an "evolutionary" versus "first-principles" approach.
11. We are not seeking a decision from you on this now. We think the best times to decide between an evolutionary or first-principles review are both as part of, or after, considering your options for the response to the Inquiry, and making decisions regarding the property markets work.
12. We do not recommend limiting ambition to a targeted reform. Reasons include:
 - EQC has been subject to a wide range of internal and external reviews since 2011. Extracting the full benefits from those, in terms of an EQC better positioned to achieve Government policy goals and deal with future claims events, will require making wide-ranging changes to the Act, even if an evolutionary approach is adopted. For instance, we expect the Inquiry to recommend that a purpose section be added to the EQC Act. Achieving the full benefits for legal interpretation of doing this would require reviewing the Act as a whole in light of the new purpose section
 - the other two approaches provide Ministers the opportunity to consider their objectives for the scheme as a whole and the role they want the EQC to play in the future, and the design that best supports those objectives, well-informed by the lessons from, and the various reviews of, recent large claims events, and
 - the appetite for comprehensive legislative reform will reduce over time. A pattern in the history of the EQC Act is that major changes have only occurred after large claims events (the 1979 Abbotsford landslip, the 1987 Edgecumbe earthquake, and the current processes following the Canterbury and Kaikoura earthquakes).

13. The two main arguments for a targeted reform are time and resources – an evolutionary or first-principles review will take longer and make bigger demands on Ministers, officials and stakeholders. However, policy analysis undertaken for the review of the Act begun in 2012, positions us well for this work. If required, an evolutionary or first principles review could be accompanied by an “early harvest” of targeted reforms. The EQC MUBs bill is a potential vehicle for any early reforms, however that would delay introduction of that bill. Diverting effort into a separate targeted reform would also likely delay the larger reform package.

Scope of Review

14. Broadly, we see an evolutionary or first-principles policy and legislative review canvassing the following areas:
- **Determining EQC’s intervention logic/ purpose/ policy objectives:** What does the Government want EQC to achieve? The intervention logic for EQC is explored in the companion report T2019/4058. Firming up the policy objectives will strongly shape our advice on design options.
 - **What EQC insures:** EQC should insure what buildings, what land, against what disasters, to what levels and on what conditions? The current work on property insurance markets will help inform thinking on this.
 - **How EQC handles claims:** How should operational and policy aspects of claims handling design be balanced? Should there be more statutory guidance on claims handling matters e.g. claimant protections? Should EQC be required to use private insurers to handle its claims? Should the Act require EQC to offer dispute resolution processes for claimants?
 - **How EQC prices its insurance:** What statutory guidance and review provisions should be included? (EQC levy rates were unchanged from 1945-2012).
 - **How EQC manages financial risks and investments:** The EQC Act predates the Acts governing other Crown Financial Institutions and the Crown Entities Act.
 - **EQC’s institutional design:** Should EQC retain all its current functions, or take on new ones? Is the governance model appropriate? Should it remain a crown entity?
 - **Technical improvements:** A raft of technical improvements have been identified, drawing on experience gained from operation of the Act to date, and various post-Canterbury reviews.

Timing and Process

15. The next few months will involve some crowded and complex decisions and interactions across several related work streams. There are also two-way interdependencies between the short-run and long-run. That is, views regarding the strategic policy purpose of the EQC scheme will shape analysis and decisions on short-run issues, and decisions on those short-run issues will inform and shape any strategic reassessment of EQC’s role and purpose.

16. The currently-envisaged timings on immediate EQC and insurance-related issues are:

Month	Response to Public Inquiry into EQC	EQC MUBs amendment bill	Insurance Affordability
March 2020	Report received.	Policy paper considered by Cabinet.	Sector consultations and development of advice.
April 2020	Oral item at Cabinet. Advice and reporting leading to Cabinet paper on 28 April.	bill drafted.	Advice on lifting EQC cap.
May 2020	Ongoing work flowing from Cabinet decisions.	LEG paper, bill introduced.	Cabinet paper reflecting decisions on April advice.
June 2020		First reading (TBC).	Likely ongoing work flowing from Cabinet decisions.
Ongoing		Passage of bill	

17. Enacting an EQC bill that is well-informed by policy analysis and stakeholder engagement requires a number of phases that, in total, are likely to spread over several years. The Treasury staff assigned to this project, at least initially, are also heavily involved in the above three projects.
18. An indicative structure and timeline is outlined below. Two processes, with and without a public discussion document, are shown, as the need for a discussion document will depend on the level of ambition or complexity of the proposed reforms.

Indicative Timing	Phase	
March 2020	This report and its companion report, T2019/4058. An upcoming report on EQC and climate change.	
To July 2020	Reporting on high-level design issues, such as what EQC insures (subject to competing demands from the other EQC and insurance projects).	
Sept 2020	General election.	
Late 2020	Further advice on design issues (this timing and the timing below is based on an evolutionary reform; a comprehensive reform will take longer).	
Early 2021	Reform package taken to Cabinet.	
Early-mid 2021	Discussion Document released (typically 6-12 weeks for submissions, more if over Christmas holidays).	No Discussion Document PCO draft bill (we anticipate PCO requiring at least 16 weeks).
Mid 2021	Consider feedback and finalise policy, Cabinet commission drafting of bill.	Cabinet approve exposure draft of bill for release, exposure draft released.
Mid-late 2021	PCO draft bill (we anticipate PCO requiring at least 16 weeks).	Cabinet approves bill as amended for introduction; bill introduced.
Early 2022	Cabinet approve exposure draft of bill for release, exposure draft released (typically 3-6 weeks for submissions).	Parliamentary process and passage.
Early-mid 2022	Cabinet approves bill as amended for introduction; bill introduced.	
Mid-late 2022	Parliamentary process and passage (assuming usual 6 months consideration by select committee).	
2022-2024	Phased implementation of new legislation (insurers have previously indicated that for major changes insurers need at least 18 months between enactment and implementation).	

Consultation and Next Steps

19. We consulted EQC on this report.
20. We would like to discuss this report with you.

Recommended Action

We recommend that you:

- a **note** officials would like to discuss the following issues with you:
 - i. our proposal that Government ambition be an evolutionary or first-principles reform of the EQC Act, i.e., not be limited to a targeted reform
 - ii. our proposal that we seek a decision from you regarding whether to proceed with an evolutionary or first-principles review of the EQC Act either as part of, or after, your upcoming decisions regarding the property markets work, and the Government response to the Inquiry
 - iii. your feedback on the proposed indicative process and timing for a future review of the EQC Act, and
 - iv. our proposal regarding how the current policy rationale for the EQC scheme will be utilised in preparing advice on residential property insurance and the findings of the Public Inquiry into the Earthquake Commission, as outlined in the companion report T2019/4058.

Helen McDonald
Manager, Earthquake Commission Policy

Hon Grant Robertson
Minister Responsible for the Earthquake Commission