

The Treasury

Treasury Advice Related to Modernising the EQC Act Information Release

December 2021

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- [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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Treasury Report: Modernising the Earthquake Commission Act:
Outstanding policy matters relating to building cover

| | | | |
|--------------|--------------|---------------------|-------------|
| Date: | 29 July 2021 | Report No: | T2021/1597 |
| | | File Number: | TY-2-1-17-2 |

Action sought

| | Action sought | Deadline |
|---|--|-----------------|
| Hon Grant Robertson Minister of Finance | Noting. | N/A |
| Hon Dr David Clark Minister Responsible for the Earthquake Commission | Agree to the proposed approach to responding to outstanding policy matters relating to building cover identified as part of drafting the bill to modernise the EQC Act. | 12 August 2021 |

Contact for telephone discussion (if required)

| Name | Position | Telephone | 1st Contact |
|-----------------|--|------------------|--------------------|
| Danijela Tavich | Analyst, Earthquake Commission Policy Team ^[39] | ^[35] | ✓ |
| 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: Yes (attached)

Treasury Report: Modernising the Earthquake Commission Act: Outstanding policy matters relating to building cover

Executive Summary

This paper seeks your agreement to a number of recommendations relating to the scope of building cover under the Earthquake Commission Act 1993 (EQC Act). These issues have been identified as part of preparing drafting instructions for the Parliamentary Counsel Office (PCO) on the Bill to modernise the EQC Act. The drafting process is well underway. That process requires consideration of the specific legal workings of policy proposals which can give rise to a need for further decisions. We expect there to be further issues identified which we will provide advice on over the coming months.

The issues covered in this paper are summarised below.

- **Whether EQC should cover building upgrades legally required prior to a natural disaster:** We seek your decision on whether EQC should be liable for the cost of building upgrades legally required prior to a natural disaster, such as earthquake strengthening for earthquake-prone buildings (EPBs). The 2017 amendments to the Building Act 2004 and the Building (Specified Systems, Change the Use, and Earthquake Prone Buildings) Regulations 2005 require EPB upgrades to be carried out where building consents for substantial alterations to a building are applied for. This could include building consents required for repairs for natural disaster damage.

We recommend the modernised EQC Act clarify that EQC cover does not extend to funding building upgrades where the legal requirement to do the upgrade pre-dates the disaster damage. In these cases, the upgrade obligation is not a consequence of the natural disaster damage, so on that basis it should be excluded from EQC natural disaster cover. This approach is in line with the private insurance policies.

We note that may mean in some cases a building with a settled EQC claim will not be able to be repaired until a building consent can be issued, which could only be done when the homeowner pays for other necessary upgrade work such as earthquake strengthening. Homeowners can access a variety of government-provided financial support to remediate their earthquake-prone buildings, such as the Residential Earthquake-prone Building Financial Assistance Scheme.

- **Clarifying EQC's treatment of common property.** We propose the EQC Act should clarify that in cases where common property is involved, EQC will meet the cost to reinstate the insured's interest or ownership in the property. This aligns with the treatment of these cases in response to the Canterbury earthquake sequence. This means that ownership interest of uninsured owners will not be counted towards the amount of EQC's settlement for any proportion of common property. We note this aligns with the status quo EQC and private insurer approach to dealing with uninsured properties.
- **Minor and technical clarifications:**
 - **Providing for a regulation-making power to prescribe measurement standards relating to mixed-use buildings.**
 - **Separating the definitions of volcanic activity and hydrothermal activity in the Act.** We recommend volcanic and hydrothermal activity should be defined as separate types of event, based on advice from GNS Science that it is possible for hydrothermal activity to occur which is not technically 'volcanic activity'.

- **Clarifying the treatment of cable cars.** We recommend that the EQC Act should clarify that cable cars can be covered. We consider this to be an important clarification as cable cars can be the main access for a property (for example on a cliffside property).

Cabinet has authorised you to make policy decisions arising during the development of the Bill [CAB-21-MIN-0177 refers]. Consequently, we consider that the majority of the decisions on the matters in this report do not require Cabinet confirmation. However, clarifying EQC's stance on common property may require a Cabinet report back as it is a slight amendment to Cabinet's previous decisions on mixed-use buildings [CAB-20-MIN-0120 refers]. We consider that report back could be done through the Cabinet Legislation Committee (LEG) when LEG considers the EQC Bill for introduction.

Recommended Action

We recommend that you:

Building upgrades legally required prior to a natural disaster:

- a **note** there may be some situations where EQC's repair of natural disaster damage may not be lawfully carried out without also upgrading a building, including upgrades legally required before a disaster occurred, such as in relation to Earthquake Prone Building regulations
- b **note** private insurance contracts generally include a provision to exclude these existing liabilities from cover

Either

- c **agree** that EQC should exclude cover for building upgrades legally required prior to a natural disaster (**recommended**)

Agree/disagree.

- d **note** that agreeing to **recommendation c** may mean in some cases a building with a settled EQC claim will not be able to be repaired until a building consent can be issued, which could only be done when the homeowner pays for other necessary upgrade work such as earthquake strengthening
- e **note** homeowners can access a variety of government-provided financial support to remediate their earthquake-prone buildings, such as the Residential Earthquake-prone Building Financial Assistance Scheme

Or

- f **agree** that EQC should be liable for all building upgrades required to ensure a building complies with any relevant laws or regulations, up to the EQC cap

Agree/disagree.

Clarifying EQC's treatment of common property

- g **agree** to clarify in the EQC Act that EQC will meet the cost to reinstate the insured's interest or ownership in common property and other shared property

Agree/disagree.

- h **note** that **recommendation g** above aligns with the approach taken by EQC in response to the Canterbury earthquake sequence

- i **note** that the clarification of EQC's stance on common property would be a slight divergence from Cabinet's agreed approach on EQC settlements for common property in non-residential mixed-use buildings – because the EQC settlement will be based on the insured ownership interest of the building, rather than residential floor area

- j **note** the change to mixed-use buildings policy may require a Cabinet report back to confirm the amendment to our approach to implementing Cabinet's previous decisions

- k **agree** that the report back should be done through the Cabinet Legislation Committee (LEG) when LEG considers the EQC Bill for introduction

Agree/disagree.

- l **note** we will work with your office to arrange this as part of preparing the Cabinet paper for LEG

Prescribing measurement standards for mixed-use buildings

- m **agree** to a regulation-making power for the EQC Act which will enable standards of measurement to be prescribed for assessing mixed-use buildings, if required in future

Agree/disagree.

Separating the definitions of volcanic activity and hydrothermal activity

- n **note** that you previously agreed to include a definition in the EQC Act with the following proposed scope [T2020/2874 refers]:

- i. Volcanic and hydrothermal activity: a sudden or continuing release of energy, gas, or other matter due to near-surface or surface magmatic processes. Includes lahar.

- o **agree** to define volcanic and hydrothermal activity as separate types of events

Agree/disagree.

- p **note** this proposal is based on advice from GNS Science that it is possible for hydrothermal activity to occur which is not technically 'volcanic activity'

- q **note** this decision means that the 7-day event period agreed for volcanic activity will not apply for hydrothermal activity, which will have an event period of 48 hours

Clarifying the treatment of cable cars

r **agree** to clarify that cable cars can be covered by EQC as an appurtenant structure.

Agree/disagree.

Helen McDonald
Manager, Earthquake Commission Policy Team

Hon Dr David Clark
Minister Responsible for the Earthquake Commission

Treasury Report: Modernising the Earthquake Commission Act: Outstanding policy matters relating to building cover

Purpose of Report

1. This paper seeks your agreement to a number of recommendations relating to the scope of building cover under the Earthquake Commission Act 1993 (EQC Act).

Building upgrades legally required prior to a natural disaster

2. The current EQC repair standard for residential buildings that are damaged as a result of earthquake or other natural disaster damage is to restore buildings to a state that is “substantially the same as but not better or more extensive than the building’s condition when new, **modified as necessary to comply with any applicable laws**”, and to do so in a “reasonably sufficient manner”.
3. In general, this means EQC cover is intended to fund natural disaster damage repairs that are compliant with the Building Act and any local planning regulations. This can often result in upgrades to the damaged home, for instance better foundations, wiring, insulation, or removal of hazardous materials such as asbestos. It is intended that the modernised Act retain this feature, which is broadly consistent with private insurance practice and the principle that the insurance or EQC cover should fund a legal repair.
4. Generally, the need to repair to current code is triggered by the need to repair the damage. There is no pre-existing obligation on the homeowner to perform remedial works to bring an older building up to current code. Therefore, the obligation to bring the damaged elements to current code flows directly from the incurring of the natural disaster damage.
5. However, EQC’s repair standard means there are some situations where the upgrade obligation pre-dates the natural disaster damage. In these cases, EQC may become liable to fund building upgrades that were legally required prior to a natural disaster event. The most likely situations where EQC may need to pay for building upgrades of this kind is in relation to earthquake-prone buildings.
6. We recommend the modernised EQC Act clarify that EQC cover does not extend to funding building upgrades where the legal requirement to do the upgrade pre-dates the disaster damage. In these cases, the upgrade obligation is not a consequence of the natural disaster damage, so on that basis it should be excluded from EQC natural disaster cover.

The EPB scheme was established following the Canterbury earthquakes

7. At the time of the Canterbury Earthquakes in 2010 and 2011, the current earthquake-prone building (EPB) scheme had not been put in place. EQC was not generally not required to meet the cost of EPB upgrades as part of its settlements, because there was no legal requirement for the upgrades to be carried out at the same time as repairs. EQC repair strategies would however sometimes contain some elements of an EPB upgrade, where damaged building elements were to be replaced with modern equivalents which complied with current code.
8. In 2017, the amendments to the Building Act 2004 and the Building (Specified Systems, Change the Use, and Earthquake Prone Buildings) Regulations 2005 came

into force. These require EPB upgrades to be carried out where building consents for substantial alterations to a building are applied for. This could include building consents required for repairs for natural disaster damage, but the interaction of these requirements with the cover provided by EQC has not been tested to date.

9. The EPB system is intended to balance complex trade-offs between life safety, heritage (culture and community identity), and remediation costs, and is based on building owners' longstanding obligations to remediate their unsafe buildings to reduce the risk of harm to others.¹ The system is predicated on building owners, not Government, having primary responsibility to remediate EPBs.
10. The regulations apply to residential buildings that are at least two storeys and either: (i) a hostel, boardinghouse, or other specialised accommodation; or (ii) contain 3 or more household units. Ministry of Business, Innovation and Employment (MBIE) analysis of data provided by Wellington and Auckland city councils suggests that the proportion of residential EPBs is around 10% of total EPBs (around 1,000 residential EPBs). However there could be multiple units and multiple owners in each residential EPB.²
11. Section 133AT of the Building Act prohibits a council from granting building consent for the alteration of a building (or the part of a building) that is subject to an earthquake prone building notice, unless, in the case of a 'substantial alteration', the alteration includes the necessary seismic work. 'Substantial alteration' is defined in regulation 11 of the Building (Specified Systems, Change the Use, and Earthquake Prone Buildings) Regulations 2005 is work that:
 - i needs a building consent, and
 - ii together with other work consented in the past two years, has an estimated value of at least 25% of the building's value and is more than \$150,000.³

Substantial building work cannot take place on an EPB unless seismic strengthening takes place

12. EPB legislation could be relevant for a post-disaster building repair if:
 - a building subject to an EPB notice is damaged in an earthquake, and
 - the repair of the natural disaster damage triggers the need for a building consent, and
 - the estimated value of the work requiring building consent exceeded both 25% of the buildings value and \$150,000.
13. In this situation, the requirement to carry out the seismic work is also triggered. While EQC's liability for the cost of seismic work would only be up to the cap, in a building with more than one dwelling (e.g. an apartment building), the cap is multiplied by the number of dwellings, i.e. currently \$150,000 per dwelling. Figure 1 demonstrates this effect.

¹ For example regarding dangerous, affected and insanitary buildings (per section 121 onwards in the Building Act).

² See MBIE report 'Early insights – Initial evaluation of the Earthquake-prone building system (March 2021)': <https://www.mbie.govt.nz/assets/early-insights-initial-evaluation-of-the-earthquake-prone-building-system-report.pdf>

³ <https://www.building.govt.nz/assets/Uploads/managing-buildings/earthquake-prone-buildings/epb-substantial-alterations.pdf>

Figure 1: EQC cap application to a standalone house versus multi-dwelling building



14. Estimates of EPB remediation costs for multi-unit apartment buildings range from \$56,000 to \$480,000 per multi-level residential unit equivalent to achieve a 34% New Building Standard (NBS) standard (2012 estimates). However, more recently, some owners have suggested that the \$250,000 maximum loan offered through MBIE's Financial Assistance Scheme (detailed further below) is insufficient to meet their needs.
15. Additionally, while the minimum remediation required to remove the EPB notice is 34% NBS, the insurance and resale market reportedly expects a higher standard, often 67% - 80%. In essence, there is a broad spectrum of cost for different building types, needs, and levels to which people might choose to strengthen, which means the actual costs of remediation are relatively unknown.
16. We have provided more information on the potential costs to EQC of remediating EPBs in Wellington in a local natural disaster event at Appendix 1.

Private insurers have changed their policies to respond to the EPB regulations

17. Following the Canterbury earthquake sequence and subsequent EPB scheme implementation, private insurance contracts generally include a provision to exclude these types of costs from cover for undamaged parts of a home. Private insurers do this by excluding:
 - compliance costs where notice of non-compliance had been served on the homeowner before the loss occurred (such as a notice of an Earthquake Prone Building)
 - the repair or replacement of any part of a building that has not suffered loss.
18. This means that where the requirement to carry out the seismic repairs has been triggered and the claim is over cap, then insurance would not cover this and the building owner(s) would need to fund the seismic works above the level of the cap.

There are other financial supports available for EPB owners

19. Homeowners can access a variety of other supports for to remediate their EPBs:
 - The Residential Earthquake-prone Building Financial Assistance Scheme (FAS) was established in 2020 to support some homeowners to remediate their EPBs. Administered by Kāinga Ora, the FAS offers low-interest loans of up to \$250,000 to unit owner-occupiers in residential EPBs, in areas of high seismic risk, who face hardship over earthquake strengthening costs. The FAS is currently undergoing a 12-month review to ensure its settings are appropriate.

- [29] and [33]

- Some councils and other agencies also offer targeted funding and support to help certain homeowners overcome barriers to remediation. Evidence indicates some funding sources are being disestablished, though remediation deadlines are still some time away – for instance, the Ministry of Culture and Heritage’s Heritage EQUIP funding has expired, while Wellington City Council’s Building Resilience Fund has been discontinued from 1 July 2021.

We recommend EQC should not cover upgrades of this nature

20. As abovementioned, we recommend the modernised EQC Act clarify that EQC cover does not extend to funding building upgrades where the legal requirement to do the upgrade pre-dates the disaster damage, as the upgrade obligation is not a consequence of the natural disaster damage. EQC excluding cover for building upgrades of this kind would be consistent with private insurer practice and the principle of indemnity. The purpose of insurance is to make good the loss – remediating building issues that existed before the loss extends beyond this.
21. A key issue that would arise if EQC excludes cover for building upgrades required prior to a natural disaster will be that homes could have a settled EQC claim but not be able to undergo repair work if a building owner was unwilling or unable to fund necessary upgrades themselves. This is because a building consent authority cannot provide a building consent for the repair work unless also satisfied that any necessary EPB remediation or upgrade work (funded by the building owner) would also take place. This could be perceived as being at odds with effectively achieving the EQC Act’s outcomes [DEV-21-MIN-0062 refers], including *‘to reduce the impact of natural disaster damage by encouraging resilience and by contributing to the timely replacement or reinstatement of residential land and buildings’*.
22. However, we consider concerns arising from cost-sharing of the EPB scheme between homeowners and Government are best addressed by programmes and supports developed by MBIE (e.g. the Financial Assistance Scheme^[29] and^[33] as this creates a single clear pathway for compliance with the EPB system.
23. If a major natural disaster damage brings forward the requirement for EPB strengthening from the statutory deadlines under the EPB scheme for a number of properties, there may be more appropriate mechanisms to ease the financial challenge for homeowners, rather than via an insurance payment. We also note that the EPB system has specified deadlines by which buildings must be remediated or demolished, so the potential risks of people living in EPBs will reduce over time.
24. Additionally, EQC funding for seismic works for some homeowners whose buildings suffered natural hazard damage and therefore were eligible for an EQC claim may create horizontal inequities between EPB owners who have and have not suffered earthquake damage. It also creates the potential for moral hazard effects whereby EPB owners are disincentivised from undertaking seismic strengthening in the anticipation of an event that may trigger EQC compensation for the works. This effect also undermines a key EPB system goal to ensure remediation takes place by the statutory deadlines.
25. There is also a risk that other Government-mandated building upgrade schemes (for example around climate change adaptation) could be put in place in future, leading to similar liability. Clarifying the EQC Act’s position on these circumstances provides

certainty around earthquake-prone buildings, but also eliminates the risk of other policy interactions like this occurring in future.

EQC could direct claimants to EPB financial supports

26. If cover under the EQC Act excludes the cost of EPB remediation, there may be opportunities at a claims handling level to direct claimants who need to undertake earthquake strengthening towards relevant funding schemes as outlined in paragraph 19 above.
27. Because EQC would likely cash settle with claimants in this scenario, the combination of the EQC settlement cost for natural disaster damage and EPB financial supports may be sufficient for homeowners to undertake the necessary repairs and seismic upgrades. This would mitigate the risks set out above about homeowners being unable to repair their buildings.

There could be a communications risk for EPB owners

28. The EPB scheme has been the subject of much public debate among homeowners on how costs of such works should be shared between public and private spheres. There is a risk that a clear exclusion for building upgrades like EPB strengthening from the EQC Act may be perceived as a narrowing of financial supports that are available for EPB owners. However, we consider this to be a minor risk as, in our view, the proposals in this paper are a clarification of the scope of EQC cover in relation to building upgrades – rather than a narrowing of the status quo.
29. If public concerns arise around the proposal, we consider this can be mitigated by emphasising the availability of wider supports such as the Financial Assistance Scheme (FAS). Further, the FAS is currently under review by MBIE, and if any required amendments become apparent as a result of public responses to the EQC proposal, those can be considered through that process.
30. Improved alignment between EQC claims handling and the EPB process is another potential mitigation, as abovementioned.

This policy decision will also have implications for EQC's treatment of council 'notices to fix'

31. Another scenario where building upgrades might be required prior to a natural disaster is when councils issue a notice to fix requiring a person to remedy a breach of the Building Act 2004 or regulations under the Act. EQC operational practice is not to compensate claimants for costs of complying with a notice to fix, though, as outlined above, the current legislation is not clear whether this approach could be challenged. Therefore, a clear decision on EQC's treatment of building upgrades relating to notices of non-compliance in relation to EPBs will also confirm EQC's status quo approach in notice to fix cases.

Clarifying EQC's treatment of common property

32. As a result of the Canterbury earthquake sequence, EQC received claims for a number of items of common property. That is, property owned jointly by the owners of two or more neighbouring dwellings. Common property can be:
 - common spaces in a building (like a lobby in a multi-unit building)
 - common building elements (like a roof on a multi-unit building)

- shared property – meaning property which is jointly owned and insured separately by one or more insurers.⁴
33. While common property is particularly relevant for multi-unit buildings, common property can also include property such as common retaining walls shared by standalone houses.⁵
34. The EQC Act recognises that some of the property covered will be common property, but does not adequately specify how claims for that property should be settled. Where more than one person has an insurable interest in property, EQC is only required to have “due regard to the respective insurable interests” when settling the claim.
35. Private insurers faced similar issues following the Canterbury earthquake sequence, and in response have generally included provisions confirming that they will meet the cost to reinstate the insured’s interest or ownership in the common property. Effectively, each insurer meets the costs to the extent of their insured’s liability. For example:
- If two insurers insure common property, and one of the insured parties would be liable to meet the full cost of reinstatement, their insurer must meet the full cost.
 - If two insurers insure common property, and each is liable for part of (likely half) the cost of reinstatement, each insurer must meet the equivalent value of their share of the claim.
36. This is the approach adopted by EQC in relation to common property. We propose the Act should clarify this to provide greater certainty on how these settlements operate. We note this will be relevant for all forms of common property owned in multi-unit buildings and by owners of standalone homes.

Implications for multi-unit and mixed-use buildings

37. Cabinet has agreed proposals intended to result in EQC better recognising the residential use of common property in mixed-use buildings (MUBs) [CAB-20-MIN-0120 refers]. The practical effect will be to, at the margin, increase the level of EQC cover of MUBs that currently do not qualify as residential buildings under the EQC Act. The changes:
- amend the **residential building test (the 50% test)**. Currently under the EQC Act, a building is a residential building if dwellings account for 50% or more of the floor area of the building. The proposal is to also count floor areas associated with residential appurtenant structures e.g. storage lockers and garages), and the proportionate residential share of common areas (e.g. corridors and lift lobbies), and
 - where a building is below the 50% test in the new residential building test, extend EQC cover to common areas on a proportionate basis, determined using the residential floor area in the building. That is, if a building is 40% residential, EQC will compensate up to the value of 40% of the damage to common areas.
38. EQC’s treatment of common property will be relevant for mixed-use and multi-unit buildings when owners are individually insured, and one or more owners have decided not to purchase insurance or have been unable to obtain it. It will also be relevant for

⁴ [25]

⁵ Note we will consider whether this policy position requires any flow-on clarifications for land cover.

mixed-use buildings insured under a single policy which do not meet the 50% test to be a residential building.⁶

39. A benefit of unit title properties as compared with other forms of ownership is that there are clear requirements under the Unit Titles Act for a body corporate to purchase insurance for the whole building. However, with some other ownership arrangements (like cross-leases), there may be no requirement to insure the building as a whole.
40. In those cases, uninsured dwellings in a building will not receive settlements from EQC. In line with this, the ownership interest of uninsured owners will also not be counted towards the amount of EQC's settlement for any proportion of the common property.
41. We note this aligns with the status quo EQC and private insurer approach to dealing with uninsured properties. It is possible that this approach could be seen as unfairly disadvantaging insured homeowners in a multi-unit building, who may feel that they cannot control the decisions of their uninsured neighbours and then face disadvantages because of other owners' decisions (that is, less EQC compensation toward common property that they are collectively liable for).
42. However, we note these problems do not stem from the EQC scheme. They stem from the particular ownership and insurance arrangements, and decisions by some homeowners to not insure. The same problems could arise following a private insurance claim for a flood or house fire (noting EQC covers land but not buildings against flood damage). We consider it is important that EQC's approach minimises potential free rider incentives for uninsured owners that could be created were EQC to provide compensation for uninsured proportions of common property.

This policy position is a slight amendment to one of Cabinet's decisions on MUBs

43. As part of Cabinet's decision on MUBs, it was agreed that:

where a building is below the 50% threshold in the residential building test, EQC cover will extend to common areas on a proportionate basis, determined using the residential floor area in the building [CAB-20-MIN-0120 refers].

44. We note that the above clarification of EQC's stance on common property would be a slight divergence from this recommendation. That is because the EQC settlement will be based on the proportion of the residential insured owners' interests, rather than the residential floor area.
45. This may require a Cabinet report back to confirm the amendment to our approach to implementing Cabinet's decisions on MUBs. We consider that, given this is a minor policy clarification, this could be done through Cabinet Legislation Committee (LEG) when LEG considers the EQC Bill for introduction. LEG may require power to act to approve this minor policy change. We seek your agreement to this approach and, if agreed, will work with your office to arrange this as part of preparing the Cabinet paper for LEG.

The interaction between multi-unit buildings without body corporates has been an issue in the on-solds space

46. We note that the underlying interaction between neighbouring properties without body corporates (i.e. outside of the Unit Titles Act) has been an ongoing issue for on-sold building repair policy in Canterbury.

⁶ In these cases, the policy will be relevant to non-residential parts of a mixed-use building (commercial spaces) for the same reasons as uninsured dwellings i.e. there is some common property, but the non-residential parts have no EQC cover. We note the non-residential parts of a building of this type may still be covered by another insurer.

47. You recently received advice on on-solds and multi-unit buildings with shared building elements [T2021/1258 refers]. The issues around repair dependencies cannot be resolved as an insurance issue, as it is primarily an issue associated with certain property titles such as cross-leases and freehold terrace housing. You will receive further advice on options to cover the cost of repairing these properties in August.

Minor and technical policy issues

48. We also seek your decision on several minor and technical policy issues relating to the scope of EQC building cover as outlined below. These include:
- Providing for a regulation-making power to prescribe measurement standards relating to mixed-use buildings.
 - Separating the definitions of volcanic activity and hydrothermal activity in the Act.
 - Clarifying the treatment of cable cars.

Providing for a regulation-making power to prescribe measurement standards relating to mixed-use buildings

49. As part of assessing whether a building meets the 50% test to be a residential building, there may be a need in some borderline cases (i.e., where a building is not obviously half residential or non-residential) for EQC to engage a building surveyor to help determine whether the residential part of the building accounts for half of its floor area.
50. EQC operational staff consider that this is expected to be low risk, as it is only in rare cases that a building is not clearly under or over the 50% test. EQC is confident that operational measuring standards can be appropriately developed to support any instances where such precise measurement is required.
51. Nonetheless, we consider that there may be instances in future where the Government may wish to prescribe clear standards in regulations to support EQC and claimants to navigate these situations. In the interests of durability of the EQC Act, we propose to provide for a regulation-making power in the Act that will enable future Governments to prescribe specific standards of measurement relating to mixed-use buildings. This may involve cross-referencing survey or valuation industry standards in the EQC Act.
52. If you agree, we will work with PCO on the detailed design of the regulation-making power.

Separating the definitions of volcanic activity and hydrothermal activity in the Act.

53. You previously agreed to include a definition for volcanic and hydrothermal activity in the EQC Act with the following proposed scope [T2020/2874 refers]:
- i. Volcanic and hydrothermal activity: a sudden or continuing release of energy, gas, or other matter due to near-surface or surface magmatic processes. Includes lahar.
54. In further consultation with GNS Science, it has become apparent that in some rare circumstances, hydrothermal activity may occur without volcanic activity. A volcano may not have erupted for thousands of years (e.g. Rotorua), but the heat from cooling magma is still sufficient to drive the hot springs and geysers at the surface – meaning there is the potential for explosive activity without new injection of magma. These kinds of events are thought to be low probability and if they do occur, are likely to be minor

and not to cause property damage. However, some damage may occur related to subsidence or gas discharges.

55. On this basis, GNS have advised that from a scientific perspective, it would make most sense to separate out hydrothermal and volcanic activity in the EQC Act. In line with this, we propose to define volcanic and hydrothermal activity as separate types of events. We will work with GNS and PCO on the final wording of the definitions.
56. We note that, in the current EQC Act, volcanic and hydrothermal activity are considered as separate types of natural disaster. In this sense, this proposal supports the status quo position. We note also that this policy decision would mean that the 7-day event period agreed for volcanic activity will not apply for hydrothermal activity, which will have an event period of 48 hours [CAB-21-MIN-0128 refers].

Clarifying the treatment of cable cars

57. In working through drafting instructions for a bill to modernise the EQC Act, it became apparent that one type of appurtenant structure that may cause confusion in future claims settlement is cable cars. This is because it is currently unclear whether a cable car would fall into the exclusion for motor vehicles in Schedule 2 of the EQC Act. We note that the definition of motor vehicle is being clarified in the new Act [T2020/3164 refers] but the lack of clarity around cable cars remains.
58. You have agreed that the status quo approach of restoring housing and appurtenances with few limits or exclusions best captures the Government's objectives for the scheme (in response to briefing T2020/3164). In line with your previous decision, we recommend that the EQC Act should clarify that cable cars can be covered, provided they meet relevant tests to be an appurtenant structure, including:
 - being permanently fixed, and
 - being in close proximity and related to the dwelling.
59. This is an important clarification as cable cars can be the main accessway for some properties (for example on a cliffside property).

Next Steps

60. If you agree to the proposals in this paper, we will prepare and issue drafting instructions to PCO for inclusion in the bill to modernise the EQC Act.

Consultation

61. EQC and MBIE have been consulted on this paper and are comfortable with the recommendations.
62. We note we have not undertaken any stakeholder consultation on the proposals in this paper. This is because of the detailed and technical nature of the proposals. There will be an opportunity to test these policy positions at Select Committee.

Appendix 1 – Earthquake-prone building (EPB) remediation cost estimates

Number of EPBs in Wellington region

Estimates from Wellington and Auckland Councils suggest around 10% of EPBs that are identified are residential buildings.

There are 586 EPBs in the register in the Wellington region. Based on the above rough estimate, this could mean 58 residential buildings. If half of these are multi-unit buildings (MUBs), that's 29 single-owner residential buildings. If the MUBs had the average of 10 units (based on the estimates provided by MartinJenkins in 2018 and potentially under-estimate in urban centres), that would mean there may be 290 units in earthquake-prone residential buildings in Wellington, in addition to the 29 residential buildings that are single-owner.

Cost estimates for Wellington region

Cost estimates to remediate an EPB range from \$56,000 to \$480,000 per multi-level residential unit equivalent.

If the remediation cost was the (low) estimate of \$56,000, then this would cost \$16.2m to remediate residential buildings in the Wellington region (56000×290).

If the remediation cost were above the EQC cap of \$150,000 and EQC therefore paid out to the cap, then this could cost \$43.5m. (150000×290).

If the cap were doubled, it would cost \$87.0m. (300000×290).

Cost estimates national picture

Based on QV estimates, it is estimated that there are a total of about 177,000 residential multi-unit buildings in New Zealand.

A MartinJenkins report to MBIE in 2018 estimated that across New Zealand there are 216 residential multi-unit buildings (with 1261 units) are in high seismic risk areas and are earthquake-prone.

If the remediation cost was the (low) estimate of \$56,000, then this would cost \$70.6m to remediate multi-unit residential buildings in high seismic risk areas in New Zealand (56000×1261).

If the remediation cost were above the EQC cap of \$150,000 and EQC therefore paid out to the cap, then this could cost \$189.2m. (150000×1261).

If the cap were doubled, it would cost \$378.3m. (300000×1261).

Caveats

- EPB remediation costs vary significantly depending on each building. This means there is significant variance in any estimate.
- The EPB register does not collate information on building usage or tenancy type, meaning it is not possible to know the exact number of identified EPBs that are residential or multi-unit. Territorial authorities may hold this information, but it is not required to be shared on the register.
- The exact number of EPBs is unknown at this stage. Priority EPBs in high seismic risk areas have been identified and are currently listed on the EPB register, but timeframes for identification extend out as far as 2032 for some kinds of buildings in some seismic risk areas.