

The Treasury

Earthquake Commission (EQC) Act Review Submissions Information Release

Release Document

January 2018

www.treasury.govt.nz/publications/reviews-consultation/eqc/submissions

Key to sections of the Official Information Act 1982 under which information has been withheld. Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

- [1] 9(2)(a) - to protect the privacy of natural persons, including deceased people;
- [2] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information.

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

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

New Zealand's Future Natural Disaster Insurance Scheme

Proposed changes to the Earthquake
Commission Act 1993

Submission Form

July 2015



THE TREASURY
Kaitohutohu Kaupapa Rawa

New Zealand Government

New Zealand's Future Natural Disaster Insurance Scheme Proposed changes to the Earthquake Commission Act 1993

Your responses

Please write your response in the template below.

Please note:

you **do not** need to answer all sections – just the ones where you have information you would like to contribute

please expand or delete boxes as you need to but **do** keep the original question numbers.

please **do not** send us reports or other documents but **do** include references or links to supporting evidence or information

please submit your response to Submissions.Eqcreview@treasury.govt.nz by 5.00pm on Friday 11 September 2015.

Thank you for your time and effort in making your submission.

Official Information Act 1982

Submissions are subject to the Official Information Act 1982 (OIA). Please set out clearly with your submission if you have any objection to any information in the submission being released under the OIA, and in particular, which part(s) you consider should be withheld, together with the reason(s) for withholding the information.

Grounds for withholding information are outlined in the OIA. Reasons could include that the information is commercially sensitive or that you wish personal information, such as names or contact details, to be withheld. An automatic confidentiality disclaimer from your IT system will not be considered as grounds for withholding information.

We will take your objections into account when responding to requests under the OIA.

Any personal information you supply in the course of making a submission will be used by the Treasury only in conjunction with the matters covered by this document. Please clearly indicate in your submission if you do not wish your name to be included in any summary of submissions that we may publish.

Your contact details

For individuals

Your name:	
	Indicate here if you do not wish your name to be included in any summary of submissions that we may publish.

Email address:	
Phone number:	

What city, town or province do you live in?	
Do you own your own home?	

For organisations

Organisation name:	TOWER Insurance
Nature of your business:	General insurance

Contact person name:	[1]
Position:	
Phone number:	
Email address:	

In what city, town or province is your organisation's New Zealand headquarters?	Auckland
---	----------

What is the purpose of the EQC scheme?

Proposal for discussion

1 That the purpose of the EQC Act be to establish a Crown-owned natural disaster insurance scheme for residential buildings in New Zealand that:

- ▶ supports, complements and is closely coordinated with the provision of effective private insurance services to the owners of residential buildings
- ▶ recognises the importance of housing in supporting the recovery of communities after a natural disaster
- ▶ supports improved resilience of New Zealand communities and an efficient approach to the overall management of natural hazard risk and recovery in New Zealand
- ▶ contributes to the effective management by the Crown of fiscal risks associated with natural disasters.

What do you think?

1a Do you agree that these purposes are appropriate and complete?

TOWER Insurance agrees that the purpose of the EQC scheme is appropriate and is aligned to the detailed ICNZ submission made in response to this discussion point.

1b If not, what changes would you suggest, and why?

What types of perils will EQC cover?

Proposal for discussion

2 That EQC continue to insure against the following perils: earthquake, natural landslip, volcanic eruption, hydrothermal activity, tsunami, and storm and flood (with, in the case of storm and flood, only residential land being covered).

What do you think?

2a Do you agree that EQC should continue to provide cover against the same perils as it currently does?

TOWER Insurance supports EQC continuing to cover the same perils as it currently does.

We note that the discussion document under the heading 'technical issues' refers to a proposal to change the definition of 'volcanic activity'. TOWER Insurance is not aware of the proposed extension of cover that is contemplated, but in principle would support a definition of this natural peril that is more comprehensive as this would minimise disputes around EQC cover. Further, and more importantly it would be important for both EQC and insurers' cover to align. Currently, TOWER Insurance provides volcanic cover that mirrors the EQC Act. More information on the change of definition is needed in order to confirm our view.

2b If not, what changes would you suggest, and why?

What types of property will EQC insure?

Proposal for discussion

3 That EQC building cover continues to be available to residential buildings and dwellings in non-residential buildings.

What do you think?

3a Do you agree that EQC building cover should continue to only be available to residential buildings and dwellings in non-residential buildings?

TOWER Insurance supports EQC building cover continuing to be available to residential buildings and dwellings in a mixed residential-commercial building where the residential component exceeds 50% of the building's use.

3b If not, what forms of accommodation or living arrangements do you think should be added or removed, and why?

As above TOWER Insurance supports EQC's proposal that EQC building cover continue to be available to residential buildings and dwellings in non-residential buildings.

TOWER Insurance also considers that holiday homes should continue to be covered by EQC. Potential complications could arise when insurers are required to distinguish between a primary and secondary residence – status quo should continue where EQC cover is applied if the holiday home is resided in at least once a year.

TOWER Insurance also supports EQC cover applying to retirement villages but not to nursing homes reflecting that they are distinguishable on the basis that one is a dwelling of choice while the other is determined by patient care arrangements. However, the line between the two may not always be that clear as care arrangements can be provided in retirement villages, so greater definition in this area is desirable.

Proposal for discussion

4 That EQC land cover only be available for land associated with residential buildings. Therefore, dwellings in non-residential buildings would not receive any EQC land cover.

What do you think?

4a Do you agree that EQC land cover should only be available for land associated with residential buildings? TOWER Insurance supports this proposal as it is a consistent and logical extension to the principle of only providing EQC cover to residential dwellings. It would be unusual to provide land cover for non-residential buildings when the purpose of the land cover is to re-house individuals after they have lost their land or it is no longer economically viable to rebuild on the land.

4b If not, what coverage of land cover would you prefer, and why?

Extending building cover to include more siteworks and main access way

Proposal for discussion

5 That EQC building cover be extended to include siteworks and the main access to the building.

What do you think?

5a Do you agree that EQC building cover be extended to include siteworks and the main access to the building?

TOWER does not support the extension of the building cover to include siteworks and main access way. It is our view that EQC should continue to cover the remediation of land, including siteworks and the main access way. Along with most other insurers, TOWER only provides cover for the residential dwelling and is not experienced in managing land claims.

TOWER Insurance believes that if this was to be implemented that customers could be dramatically exposed to the risk of being under-insured as a result of the proposal to combine site works as part of the building cover. This results from operating in a sum insured environment where the onus of estimating the appropriate level of insurance rests with our customers. For instance, in Wellington, where many homes are located on hillsides, homeowners could not or would not be able to estimate their siteworks costs. A geotechnical survey may be needed that would include the taking of one or more core samples for analysis.

The insuring public have little experience of quantifying building costs and while various sum insured calculators ask questions on slope of section, retaining walls and pathways they will not be able to provide information for the problem sites. Even if problematic sites were known (which they will not always be), they would require a site specific assessment of likely siteworks costs - an expensive proposition for a homeowner to arrange. Indeed, the amount of cover required would in turn depend on the nature of the natural disaster event and severity. It would be highly likely that siteworks would be grossly underestimated which would result in a much lower amount being left available to build or repair a house. This leaves insureds in the invidious position that for each location it will be unknown what portion of the deductible will be available for the building because they will not have been able to determine in advance the likely site work costs.

EQC's cap could be completely used up on complex siteworks. If that occurred then the sum insured remaining for the rebuild of the dwelling may not be sufficient. For example in the case of say, an \$800,000 sum insured home, if \$200,000 is spent on siteworks then only \$600,000 would remain to build an expected \$800,000 home. By including the siteworks in the EQC cap the risk of any shortfall, currently held by EQC, would fall on the homeowner.

The proposal as it stands also requires TOWER to offer cover for land or 'earthworks' which we currently do not provide and have no experience modelling for. The EQC deductible applicable to the building has a very significant impact on the level of residual risk that insurers are taking and this impact operates in a geared manner. Not knowing the amount of the deductible applicable to the building is thus a material problem from a risk and pricing perspective which will result in detrimental results for the homeowner.

Furthermore, EQC has not been able to provide any data on separate sitework costs thus making any attempt at correctly pricing such cover impossible. [2]
[2]

TOWER Insurance is prudentially regulated by the Reserve Bank of New Zealand under the Insurance (Prudential Supervision) Act 2010 and as part of that oversight the Bank requires TOWER to work within solvency standards regulating that sufficient reinsurance be held to allow for a 1 in 1,000 year event. To determine what that exposure might be insurers use earthquake models developed by recognised modelling companies. At present the available earthquake models cannot account for site works. To allow any degree of confidence in the modelled results to be given to the private insurers' Appointed Actuaries (who are responsible under the Act to determine the 1 in 1,000 year event limit) the modellers will be required to disregard the EQC cap to some extent to allow for the fact that in some cases private insurers will be covering the rebuilding cost from ground up rather than with the EQC deductible. This will increase the modelled loss resulting in higher reinsurance premiums which will ultimately work through to homeowners.

The proposal in the discussion document would also likely lead to more cash-settled, total constructive loss situations because siteworks would be significantly underestimated. Overall, this proposal shifts all the risk to the insured who would not be in a position to manage their reinstatement as well as would otherwise be the case.

Further, with the proposal for the building cover to include reinstatement of the main access way and retaining-walls the situation becomes more complex and likely a lot more expensive. Rebuild modelling is based around the rebuild of the dwelling itself and does not include retaining-walls and access ways. Modelling retaining-wall costs are particularly challenging in part because many of these have shared ownership. There is also a lack of clarity around access ways, for instance, would a crack on a small part of an access way require a rebuild of the entire access way?

In addition, homeowners will also face the challenge of estimating the complex overlay of costs associated with demand surge inflation during a recovery period that could last as long as five years.

While it might be possible to model damage over a wide area based around average losses, it will not be possible without detailed site specific inspections to estimate rebuild costs. This means that even though modelling might solve some of the problems that arise from a single building cover, the insured would still remain significantly exposed to underinsurance which runs counter to the objectives of reform.

TOWER Insurance submits that the solution to these problems lies in EQC continuing to provide land cover (up to the maximum value of the land) and that insurers handle the claims, passing the 'siteworks' or what we believe should be more appropriately called 'landworks', which reflect the costs to reinstate the building, and that these would fall back to EQC.

A tight definition of what constitutes landworks is required to ensure these cost can be readily identified. The building cover would be capped at \$200,000 and the landworks cover would be limited to the value of the land.

TOWER's view is that landworks should be defined to include (and be limited by the economic value of the minimum land area that a local authority would consent property to be built on):

- All technical testing including geotechnical testing required to inform what has to be done to the land to enable a rebuild/repair to occur
- All land remediation work required to enable a property to be repaired or rebuilt consistent with a cost effective land-foundation engineering solution – includes removal of spoil (liquefaction, volcanic ash, etc) and removal of potentially dangerous elements such as rocks
- All retaining-wall reinstatements necessary to enable a rebuild or repair to proceed consistent with a cost effective land-foundation engineering solution.
- Ground preparation for main access way
- Drainage including soak pits
- Costs to comply with hazards (under section 71-74 of Building Act)
- RMA compliance
- The notional cost of all of the above in the event of a cash settlement of the building.

Such an approach would address several frictional issues that have arisen in Christchurch. First, it removes the need for EQC to calculate factors such as increased vulnerability to flood or liquefaction as the land reinstatement issues are directed solely at the ability to repair or rebuild which is the primary objective of the scheme. Second, it removes the current difficulties insurers are experiencing with EQC over whether it will contribute to earthworks that have been carried out in order to progress repairs and rebuilds based on cost effective engineering land remediation-foundation solutions. Third, it describes how cash settled properties can be fairly compensated for land loss.

5b If not, what do you think should be done instead, and why?

EQC to no longer provide contents insurance

Proposal for discussion

6 That EQC no longer offer residential contents insurance.

What do you think?

6a Do you agree that EQC should no longer offer residential contents insurance?

TOWER Insurance supports this change and will be able to absorb this additional risk for our customers. Further, a purpose of the Act is to focus on reinstatement of residential dwelling post catastrophe, and compensation for contents damage below \$20,000 is not central to that purpose.

Clarity is sought on those items considered to be or not to be contents. Items such as landlord's chattels and carpets and drapes could be considered either a house component or contents depending on an individual insurer's wordings.

TOWER recommends that EQC cover follows the individual insurer's policy as a solution to what is covered under building or contents cover (rather than seek to define this in the Act).

6b If not, what level of contents cover do you think EQC should offer, and why?

6c For insurers, what do you anticipate the impact would be on premiums your company charges for residential contents insurance, if EQC no longer offered residential contents insurance?

Please note the information in section 1.4 regarding the Official Information Act.

[2]

How much insurance will EQC offer?

Proposal for discussion

7 That the monetary cap on EQC building cover be increased to \$200,000 + GST.

What do you think?

7a Do you agree with the proposed increase in the building cap to \$200,000 + GST?

TOWER Insurance supports an increase in the cap from the current amount of \$100,000 to \$200,000 + GST.

TOWER's view is predicated on our point noted above that it is our very clear view that siteworks cannot be included in a single statutory cap and that EQC should continue to provide cover for land. If this is accepted by Treasury we would continue to support a \$200,000 otherwise if siteworks was to be included then we would advocate for an even higher cap.

7b If not, what cap would you prefer, and why?

7c Do you have strong views on the merits of a \$150,000 + GST cap versus a \$200,000 + GST cap?

Yes, TOWER's strong preference is for a \$200,000 cap – we consider that this reflects an appropriate level of EQC cover given the average cost in Christchurch to reinstate homes as well as the fact that the amount of the EQC cap was never indexed to allow for inflation.

7d If so, what are they?

See 7a above

7e For insurers, what do you anticipate the impact would be on premiums your company charges for residential property insurance, if the proposals in this document regarding changes to building cover were implemented? Please provide this information for a monetary cap for EQC building cover of both \$150,000 and \$200,000.

Please note the information in section 1.4 regarding the Official Information Act.

[2]

Assuming that site works are excluded from the \$200,000 cap, [2]

[2]

Reinstatement of EQC cover after an event

Proposal for discussion

8 That EQC building cover reinstate after each event.

What do you think?

8a Do you agree that EQC cover should reinstate after each event? If not, what is your preferred alternative, and why?

TOWER Insurance agrees with the discussion document on this point and is a strong advocate of the proposal that EQC cover should reinstate after each event as per the High Court declaratory judgement.

Loss modelling without reinstatement would be difficult for insurers (i.e., how much would you be allocating to each possible event) and whilst possible, [2]

[2]

8b Do you agree with retaining the current definition of an event?

TOWER Insurance agrees with retaining the current definition of an event at 48 hours but is also happy to consider alignment to commercial practice of 72 hours.

8c If not, what is your preferred definition, and why?

EQC land cover

Proposal for discussion

9 That land cover be limited to situations where the insured land is a total loss meaning it is not practicable or cost-effective to rebuild on it.

What do you think?

9a Do you agree that the proposed enhanced building cover, combined with restricting land cover to situations where the site of the insured building cannot be rebuilt on, would resolve, for future events, many of the recent difficulties with the interaction between land and building cover?

TOWER Insurance does not believe that the proposed enhanced building cover (combined with restricting land cover to situations of the insured building cannot be rebuilt on) will resolve, for future events, many of the recent difficulties.

For the reasons outlined above in section 5 in relation to siteworks/landworks, TOWER Insurance does not believe siteworks/landworks can be included in one combined cap with building cover. This means that it is equally inappropriate to limit land cover to situations where the land cannot be rebuilt on. Homeowners who suffer land damage and require siteworks to be carried out still require land cover even though they fall short of a “total land loss” situation.

Instead, TOWER Insurance is aligned to ICNZ’s view that the solution to this siteworks and land cover issue can be resolved as outlined below:

- Legislative clarity is required around what constitutes siteworks/landworks and what structures EQC covers. ICNZ’s view is that siteworks/landworks must include all work (as defined in section 5), including ground-testing, professional advice, design solutions, earthworks and actual on site work, that is required to enable the repair or rebuilds. Insurers do not insure land as a matter of course.
- Insurers and their experts should manage the claim and when costs which fall within this clear definition are incurred then those are EQC’s responsibility.
- The total amount of EQC’s liability for siteworks/landworks will always be capped at the amount that EQC could be called upon to pay if the land itself cannot be built on (see below)
- The determination of whether a cost incurred on a site is dwelling or siteworks/landworks-related is a question of fact in each case and the insurer and loss adjuster responsible for managing the site are in the best position possible to determine this (subject of course to audit by EQC).
- This approach provides a holistic site-specific view and eliminates duplication of resource (in terms of both time and cost). One set of experts would review the damage to the property and its land and make a recommendation as to reinstatement which would then translate into a scope of works from which the siteworks/landworks costs could be separated for EQC to pay and the remainder of the costs are divided between EQC (up to its cap) and the remainder to the insurer.
- Siteworks/landworks should encompass either “true” siteworks/landworks such as land remediation or a different and more economic approach such as more extensive foundations, depending on what is required at the site.

Appurtenant structures

TOWER Insurance propose that the EQC cover follow that of the insurers’ policy, that is, whatever appurtenant structures are covered by the insurer would be covered by EQC. This would avoid any need for a definition of an appurtenant structure or a list of structures included/excluded and again reduces friction for the householder between EQC and private insurance cover.

9b If not, what is your preferred alternative, and why?

9c Do you agree that restricting land cover to situations where the site of the insured building cannot be rebuilt on is appropriate, given the EQC scheme's focus on providing homeowners the resources to repair, rebuild or re-establish homes elsewhere?

As above, it is TOWER Insurance's view that land cover should not be restricted to situations where the land cannot be rebuilt on. It is our view that siteworks/landworks should be a separate component of EQC money available to redress land issues up to the maximum that would be paid if the land was a total loss.

The critical issues though that arise around this proposal are what determines whether land cannot be rebuilt on and who makes that determination?

Where land has totally disappeared (as in a landslide or cliff collapse) the inability to rebuild in situ is clear and that is why land compensation was introduced to the EQC scheme after the 1979 Abbotsford disaster. TOWER would argue in the interests of certainty for homeowners that this would also apply in a situation where there is imminent loss of land. We understand that EQC defines this as a loss that in the balance of probabilities will occur within 12 months.

While physical loss of land is clear, it is not clear how it will be determined that it is not economically feasible to repair or rebuild in situ. A pure economic approach would argue that the trigger for economic loss would be if the additional cost of repair or rebuilding the dwelling on the damaged land value that arose because of the cost of remediating damage to the land, exceeded the value of the land.

The second issue is who determines whether the trigger has been reached. TOWER acknowledges that EQC, as the provider of land cover, clearly has a mandate to make that determination where it is not possible to repair or rebuild on land. However, it is less clear when it comes to determining the economic feasibility to repair the dwelling on badly damaged land. If an insurer (or homeowner) believes a repair can be carried out at less cost than a total loss then it will object to EQC determining that it is not economically feasible to do so. At the very least, if EQC were to be determining economic feasibility, it would need to be informed of the building repair costs by the insurer.

TOWER Insurance believes criteria should be drawn up irrespective of who decides whether land is an economic loss and these should clearly relate to whether the dwelling can be repaired or rebuilt on the land. TOWER's view is that the determination of economic viability should only arise if the homeowner or insurer has decided not to reinstate on the land.

There is a stronger case for the insurer to determine the economic feasibility of rebuilding or repairing in situ. This is because the economic feasibility hinges entirely upon the costs that the insurer is responsible for on the assumption that such properties will be over cap as is almost certainly the case where land has been badly damaged. In these circumstances, EQC's liability with respect to repair of the dwelling is not material to the decision. EQC's liability with respect to land cover is for total loss only, but the economics of a feasible repair are determined solely by the insurance policy and the insurer (or homeowners) ability to reinstate an insurable property.

9d If not, what is your preferred alternative, and why?

9e Do you have any concerns regarding the proposed change to the configuration of building cover in light of the move by most insurers to provide sum insured home insurance policies?

We have already covered this point by highlighting the concerns that arise under the proposal to combine siteworks/landworks and building under the one cover. This increases the risk of under-insurance in a sum insured environment.

As insurers have never insured land, proposed changes to land cover and the transition to sum insured do give rise to significant concerns under a single siteworks/landworks and dwelling cover as outlined above.

Concerns could arise for the Crown if there was significant under-insurance which meant that after a disaster there was insufficient funding to rebuild from the combined EQC and private cover. The key question is whether homeowners will have sufficient access to advisers to enable them to determine an appropriate sum insured [2]

[2]

9f If so, what is your preferred alternative, and why?

Better aligning EQC and private insurers' standard of repair

Proposal for discussion

10 That EQC's current statutory repair obligation already appears broadly consistent with industry practice.

What do you think?

10a Do you agree with the Government's assessment that EQC's legislated standard of repair is broadly consistent with current industry norms?

TOWER disagrees with Government's assessment that EQC's legislated standard of repair is broadly consistent with industry practice. Under the current Act, EQC building cover is for replacement value, meaning "any costs which would be reasonably incurred in respect of ... replacing or reinstating the building to a condition substantially the same as but not better or more extensive than its condition when new, modified as necessary to comply with any applicable laws". TOWER agrees that this standard, on its own, broadly aligns with the standard usually applying under private insurer provisions, and includes a "reasonableness" qualification often (but not always) found in private policies.

However, where EQC reinstates, EQC's obligation is subject to the qualification that it "is not bound to replace or reinstate exactly or completely, but only as circumstances permit and in a reasonably sufficient manner" (Condition 9(1)(a) of Schedule 3). This type of qualification is not usually found in private policies, so the standard of reinstatement under the private policies does not differ depending on whether the insurer elects to reinstate.

This qualification on the standard to be met when EQC repairs is vague and at odds with the standard otherwise contained in the Act, which is in any event already subject to a reasonableness requirement (as replacement value only covers costs which would be “reasonably incurred” in reinstating). There does not appear to be any good reason for the standard applying to EQC cover to differ depending on whether EQC elects to reinstate.

It is submitted by TOWER Insurance that the most effective way to minimise these tensions between EQC cover and private insurance cover is for EQC to adopt a reinstatement standard which aligns to the private insurance policy on the particular site irrespective of whether claims were under or over cap. Most wordings are relatively standard in the market and economic and market tensions would suggest that broad alignment is likely to remain the status quo. This has the advantage of removing friction between EQC and private insurer cover and the various problems that this has created as outlined above. This would also fit squarely with insurers’ management of claims and remove any bias for assessors as they would be applying the same standards across the site regardless of whether a claim is under or over cap.

If, however, this were not acceptable to the Government (that EQC follows the insurer’s policy), TOWER Insurance submits that the qualification in Condition 9(1)(a) should be deleted from the Act in order to more closely align the cover provided by EQC and private insurers. This though is a sub-optimal solution.

10b If so, do you have views on why EQC’s standard of repair is seen as markedly different from current insurance industry norms?

See the comments above. In addition, if insurers were responsible for assessing both under cap and over cap claims as is anticipated in future, the demarcation between EQC and insurer assessments would be removed by adopting our recommendation.

It is common practise in the insurance industry for insurers to be spending reinsurers and shareholder’s funds to meet liabilities. This is no different for EQC with the bulk of EQC’s liabilities being met through reinsurance arrangements – absent a rebuilt Natural Disaster Fund. Audit of insurers handling of claims is a core competency of reinsurers who would be auditing EQC claims as well as insurers. As long as there were clear audit processes available to EQC there should be no concerns about insurers’ managing under cap claims.

Although EQC and insurers have a liability to ensure repairs are of a standard that meets policy obligations, it is the insurer that has an ongoing interest in the integrity of repairs because they take on the all perils cover after their completion. This provides a stronger incentive for insurers to be satisfied about the quality of repairs and reinforces the case for insurers to handle both under and over cap claims.

10c If not, do you have suggestions for reforms that you consider would move the EQC standard of repair closer to current insurance industry norms for residential property?

Simplifying EQC's claims excess

Proposal for discussion

11 That EQC has a standard claims excess of \$2,000 + GST per building claim.

What do you think?

11a Do you agree that EQC's building claims excesses should be standardised and simplified to a flat dollar amount?

TOWER Insurance agrees that EQC's building claims excess should be standardised and simplified to a flat dollar amount but advocate that this amount should be affordable for homeowners.

It is important that our customers are able to understand their own obligations as well as those of EQC, so a move to a simpler, standard excess is required.

In light of the intention for insurers to manage claims on behalf of EQC in future, care will need to be taken to ensure that excess collection by insurers on behalf of EQC is robust. Insurers are well equipped to settle claims with deduction of appropriate excess as this is what occurs on each and every claim, whether for natural disaster claims or otherwise. The problems EQC had encountered in Canterbury in seeking to recover excesses post-repair were not an issue for the private industry as insurers discussed how to treat excesses with customers at the outset and included the option of allowing the customer to choose a reduced repair/rebuild to the value of the excess.

11b If yes, do you agree that \$2,000 + GST is the appropriate claims excess on building claims?

The purpose of an excess is to keep the overall premium costs down by enabling the homeowner to retain some of the risk rather than transferring it entirely to the insurer. It also encourages homeowners to mitigate risks for themselves, such as, removing chimneys or securing contents. As the primary purpose of the EQC scheme is to enable people to be rehoused after a disaster, it is important that the scheme be designed to that end. By maintaining a modest excess, it keeps EQC levies lower than they would otherwise be and recognises that repairing cosmetic damage to property is not the purpose of the scheme. Insurers' focus post disaster should be on handling larger claims on EQC's behalf of their own, not on very minor damage.

It is TOWER Insurance's view that the excess should be a set amount that is affordable for homeowners whilst balancing its intent. We therefore advocate for a standard excess amount that does not exceed \$2,000 + GST per event.

11c If not, what would you prefer, and why?

Proposal for discussion

12 That EQC have no claims excess on land claims.

What do you think?

12a Do you agree that EQC should have no claims excess on land claims?

Given our assertion that EQC should continue to provide cover for land damage, TOWER Insurance is open to an excess being charged for this cover. We do however also assert that the primary purpose of the EQC scheme is to enable people to be rehoused after a disaster and

therefore any excess applied to land remediation must be considered in conjunction with the excess applied to the EQC building cover in terms of affordability for homeowners.

12b If not, what would you prefer, and why?

Regularly reviewing main monetary settings of cover

Proposal for discussion

13 That the EQC Act require monetary caps, premium rates and claims excesses on EQC cover to be reviewed at least once every five years.

What do you think?

13a Do you agree that monetary caps, premium rates and claims excesses on EQC cover should be reviewed at least once every five years?

TOWER Insurance concurs with this recommendation because it enables a review to be conducted with greater frequency than every five years if the situation demanded. Global catastrophes may occur, as they did 2010-12 and were on such a scale that reinsurance costs rose very sharply worldwide. It is conceivable that similar circumstances could arise again and it would be necessary to adjust premiums to reflect changing market conditions. Having said that, TOWER Insurance would not support more frequent reviews than 5 yearly unless there was strong market volatility or similar impact because premium rate changes give rise to system and process changes which add to compliance costs.

A key matter to be addressed will be who will carry out the review and what consultation process will there be. Our expectation is that insurers would be included in a consultation process.

TOWER Insurance would like to have established lead times on the review to allow us to adequately take into account and implement any actions necessary. The cost of changing the processes and systems within an insurance company on a regular basis would be prohibitive so drastic changes more frequent than 5 years would be a burden.

13b If not, what alternative would you prefer, and why?

How will homeowners access EQC insurance cover?

Proposal for discussion

14 That EQC cover continues to automatically attach to fire insurance policies on residential buildings, as defined in the EQC Act.

or

15 That EQC cover automatically attach to insurance policies on residential buildings, as defined in the EQC Act, on a peril by peril basis; so if a peril covered by EQC is excluded from the private policy, it is also excluded from the EQC cover.

What do you think?

14a Do you agree that EQC cover should continue to automatically attach to fire insurance policies on residential buildings? Or

TOWER Insurance strongly favours the status quo point of attachment of EQC cover to fire policies.

15a do you agree that EQC cover should automatically attach to insurance policies on residential buildings, and EQC cover should exclude any natural disaster peril that is excluded from the fire insurance policy it attaches to?

15b If you do not agree with either of these options, what alternative arrangement do you prefer, and why?

Proposal for discussion

16 That EQC continue to have the ability, but not the obligation, to directly provide EQC cover to homeowners who request it.

What do you think?

16a Do you agree that EQC should continue to be able, but not be obliged, to directly provide EQC cover to homeowners who request it?

TOWER Insurance agrees with this approach

16b If not, what alternative arrangement would you prefer, and why?

Who will handle EQC claims in future?

Proposal for discussion

17 That all EQC claims be lodged with claimants' private insurers.

What do you think?

17a Do you agree that EQC claimants should be required to lodge all EQC claims with claimants' private insurers?

TOWER Insurance strongly supports this proposal and believes equally strongly that we should handle all under cap as well as over cap claims to the point of settlement or reinstatement. This would remove duplication of costs, confusion for our customers and provide them with one point of contact along with a faster recovery process.

If this was done in conjunction with EQC following the insurers' cover the vast majority of problems that arose around assessment and the intersection of EQC and private insurance cover would be removed. It would ensure recovery in future is quicker than what has been experienced in Canterbury.

Based on TOWER Insurance's experiences, along with a number of independent reports and surveys conducted on the Canterbury recovery we advocate that there should be significant change in this area.

In particular, duplicate loss assessment has led to confusion and less efficient settling of claims. It has also placed significant drain on finite resources such as engineers, builders, assessors etc. The case for change is too compelling for the status quo around claims management to continue.

Insurers have ongoing customer relationships with residents. When claims are lodged they are able to confirm cover. This is far more efficient and straightforward for homeowners than the current approach where claims are lodged with EQC initially and then EQC seeks verification from insurers whether there is cover over the property. Such an approach, would give reinsurers transparency around policy cover with none of the frictional inefficiencies that exist under the current dual claims management/assessment model. Naturally, EQC would need to have visibility of those claims in relation to managing its exposure.

Prior to the Canterbury earthquakes EQC had about 24 staff which reflects that in business-as-usual circumstances its optimum staff level cannot cope with a major disaster without a major scale up of operations. While the scale of the Canterbury disaster tested private insurers' resources too, business-as-usual for insurers involves having several thousand staff employed throughout the country. It is noteworthy that private insurers lodge, assess and settle in excess of around 1,000,000 claims a year as a matter of course. Insurers would have significantly more qualified resources and better systems in place to respond to a major disaster vis-a-vis EQC.

In addition, if insurers were also responsible for assessments, then it would ensure that all over cap claims are identified much earlier – insurers are still receiving over cap claims five years after the first of the Canterbury earthquakes.

If the Crown agrees, this would mean insurers would be assessing under cap dwelling damage on behalf of EQC. Clearly, there would be contractual arrangements with EQC and an appropriate claims handling fee agreed which would include the ability for EQC to audit under cap claims processed by insurers.

The discussion document on page 38 lists five areas the Crown will need to have confidence are addressed for outsourcing arrangements to be agreed to. The commentary below addresses some of these areas.

The first is robust audit and accountability mechanisms to manage the financial costs and risks of outsourcing claims. Private insurers have long established mechanisms to deal with just such needs with their reinsurers over treaty claims where reinsurers share risk exposure. It would be relatively straightforward to reflect similar arrangements with EQC in respect to under cap claims.

The second area is the need to have clear agreements about the quality of service provided to EQC claimants as well as ongoing accountability arrangements. Insurers have signed up to comply

with a revised Fair Insurance Code from 1 January 2016. This sets high standards of responsiveness to claimants setting timeframes for acknowledging, determining and keeping insureds informed about the progress of all their claims, including those related to natural disasters. It also sets sanctions for non-compliance. The Code's high benchmark for claims management will ensure that all insurers are operating to industry best practice standards in business-as-usual and catastrophe response situations.

And with respect to the quality of repairs and liability for them, these issues can be addressed in a straightforward manner in much the same way as they have been dealt with the establishment of Project Management Offices in Canterbury for insurer-managed repairs and rebuilds. It is important to remember that it is as much in the interests of insurers as it is homeowners to have repairs and rebuilds meet accepted building standards as insurers will want to continue to insure those properties and meet their obligations to customers.

The third area is that there are robust arrangements between EQC and insurers for sharing relevant customer and claims data in a timely and secure way. Insurers acquire privacy waivers when policies are taken out and renewed that enable some key information to be shared to settle claims, but EQC does not obtain this waiver. It would be a simple matter for the new legislation to put it beyond doubt that EQC and private insurers have a legislative mandate to share policy and claims information. This would enable a high quality match up of property, policy and owner information that are essential for claims handling.

As we have noted above, if EQC policy followed that of insurers on a per-site basis and insurers also managed the under and over cap claims homeowners would receive seamless cover and duplication of resource and cost would be eliminated. EQC would have audit ability and so could access any insurance policy documentation to investigate how the claim has been settled. This is precisely what has happened with respect to insurer-reinsurer arrangements in Canterbury for all over cap claims so is not without precedent or unfamiliar to the industry (or EQC for that matter in terms of its own reinsurance arrangements).

The fourth area is that insurers have ongoing capability and quality of preparation to manage future events. As noted earlier, insurers have thousands of staff, respond 24/7 to claims and handle over one million claims a year under business as usual. In short, insurers' response capability will always be better resourced from the get-go than EQC operating under business as usual when a major disaster strikes.

It is important to note though that TOWER Insurance would need to have a commercial arrangement with EQC for the reimbursement of costs associated with managing under cap claims. This would need to be established up-front before any claims were handled.

17b If not, what alternative arrangement would you prefer, and why?

Deadline for reporting claims

Proposal for discussion

18 That the current three-month time limit for claims notification be retained, but EQC be able to accept claims up to two years after an event, unless doing so would prejudice EQC.

What do you think?

18a Do you agree that the current three-month time limit for claims notification should be retained, but EQC should be able to accept claims up to two years after an event, unless doing so would prejudice EQC?

TOWER Insurance supports the current three-month time limit for the notification of claims. This supports an efficient and effective response to a disaster as an open-ended arrangement simply leaves claims in limbo which is in no one's best interests.

Three months is a sufficiently long time period for claimants to be able to manage through the immediate aftermath of a disaster without having to notify a claim and also long enough for owners to be aware of the damage to their properties. Under the proposal to legislate for claims to be lodged with insurers, we suggest the Act be amended to reflect this.

TOWER Insurance also acknowledges that it is possible for some damage not to be easily identifiable after an event, particularly where parts of a dwelling may not be easily accessed. And after a particularly large event, it may take some time for full assessments to be completed and damage identified outside the three-month period for notification. We understand that the Act gives EQC no discretion to accept claims in these circumstances.

TOWER Insurance believes that the key issue is to notify that some damage has occurred. The actual process of quantifying and repairing the damage can come later.

The discussion document proposes to amend the Act to allow EQC to accept notification of claims up to two years after an event period as an absolute time limit. This would provide flexibility to address the problems identified in the examples above, so we agree that EQC should have the discretion to accept claims up to two years after notification.

TOWER Insurance assumes that if the intention is that claims be lodged or notified to insurers that the Act would be worded to reflect the notification time as the time notification is made to the insurer, not EQC. There would of course need to be an obligation on the insurer to in turn notify EQC.

18b If not, what alternative arrangements would you prefer, and why?

Ensuring the scheme meets its expected costs

Proposal for discussion

19 That the new EQC Act contain pricing and transparency principles requiring the scheme to adequately compensate the Crown for its expected costs and risks.

What do you think?

19a Do you agree that the new EQC Act should contain pricing and transparency principles requiring the scheme to adequately compensate the Crown for its expected costs and risks?

TOWER Insurance agrees that clear pricing principles stated up front would ensure the scheme was sustainable and give insurers and customers more certainty around how the scheme would respond in the event of a disaster.

19b If not, what alternative arrangements would you prefer, to ensure the scheme's future financial sustainability, and why?

Allow but do not require differentiated EQC premiums

Proposal for discussion

20 That the current legislative flexibility to charge flat-rate or differentiated EQC premiums be retained.

What do you think?

20a Do you agree that the current flexibility to charge flat-rate or differentiated EQC premiums should be retained?

TOWER Insurance prefers a simple pricing structure which makes it easier to explain to customers and be supported in systems. For that reason the flat rate is preferred as noted in the submission from ICNZ.

20b If not, what alternative arrangement would you prefer, and why?

20c Do you agree with the Government's intention to continue charging EQC premiums at a universal flat rate?

How will EQC finance its risk?

Proposal for discussion

21 That the Natural Disaster Fund be retained in broadly its current legislative form.

What do you think?

21a Do you agree that the Natural Disaster Fund should be retained in broadly its current legislative form?

TOWER Insurance agrees that the Natural Disaster Fund should be retaining broadly in its current form.

21b If not, what changes would you like to see considered?

Proposal for discussion

22 That the Act enable EQC to use other forms of risk transfer, in addition to traditional reinsurance.

What do you think?

22a Do you agree that the Act should enable EQC to use other forms of risk transfer, in addition to traditional reinsurance?

Do you have any other feedback?

Other feedback

23a Are there any issues not discussed in this document that you would like to bring to the Government's attention at this stage?

23a Are there any issues not discussed in this document that you would like to bring to the Government's attention at this stage?

Yes, there are a number of issues raised under the subject of Technical Issues on page 45 of the discussion document we would like to comment on. These largely focus on the matters that would better align the EQC Act with private insurance practise.

Also, there are issues that need to be addressed in other legislation which would support a more efficient and effective recovery post-disaster that should not go ignored by virtue of a focus on the EQC Act (the Unit Trusts Act is an example).

23b What submissions would you like to make on those issues?

A.1 Enable EQC to deny claims where the private insurer has declined for the same natural damage

The current Act does not enable EQC to decline claims in every case where a private insurer has declined a claim for the same damage.

This would be particularly important if insurers were acting on behalf of EQC to handle under cap

claims. So, if the insurance policy is avoided for any reason then EQC cover does not apply. However if the claim is declined by the insurer then EQC cover may still apply depending on the reason for declination.

Private insurers may decline claims for changes of building use prior to the natural disaster or for fraud or other instances that might void a contract. The Act should be amended to enable EQC to decline a claim where the insurer has done so for the same natural disaster damage. Similarly, EQC should be able to recover payments if these have been made before it becomes aware of circumstances such as a change in use of the building or fraud.

TOWER Insurance would also support amending the Act to make it clear that EQC claims can be declined where the insured has not taken reasonable precautions to look after the safety of the property that has sustained natural disaster damage. This too aligns with private insurance practise.

A.2 Assignment of benefits of a claim

The Act needs to specifically contemplate and permit the assignment of claims to insurers. This would provide certainty for insurers when undertaking repairs and rebuilds to progress recovery efforts and would reduce potential frictional issues with the EQC.

A.3 Payments to mortgagees or insurers

The Act presently provides EQC with no clear ability to make payments to mortgagees or direct to insurers who are arranging reinstatement following an over-cap claim. Problems have resulted from owners spending their EQC payments on expenses other than reinstatement and have then not had funds to complete the repair or rebuild of their home.

It is also administratively burdensome for insurers to have to collect funds from owners when, with careful drafting for the appropriate situations, provision could be made in the Act for payments to be made direct to insurers or mortgagees.

A.4 Confusion over insurable interest and who may claim – section 29

In addition to the issue noted above about who may receive payment for a claim, a related issue is who may make a claim.

“Section 29 provides that:

- (a) a claim may be made in respect of any insurance under this Act only by a person who has an insurable interest in the property concerned; and
- (b) without limiting section 31, where more than 1 person has such an insurable interest, the Commission shall in settling any claim have due regard to the respective insurable interests.”

It is not uncommon for multiple insurance policies to be taken over a particular property and the Act could be clearer as to EQC’s obligations in this regard. For example, a tenant and a landlord may each take out a policy, or a unit owner and a body corporate may also each take out a policy. TOWER Insurance submits that the rights of policy holders to claim in this situation should be clarified as part of the amendments in relation to who has standing to receive payments from EQC.

A.5 The value of EQC settlement to be based on actual, final costs to repair quantified at time of settlement

Condition 13 of Schedule 3 of the Act provides that EQC may settle any claim “on the basis of the amount it would have cost to replace or reinstate the property at the time of the occurrence of the natural disaster damage to the property” and only leaves a discretion for EQC to pay on the basis of the value of the property at the time of settlement of the claim. This is at odds with private insurance policies where insurers cannot elect under replacement policies to assess payments based on what it would have cost to replace or repair at the time of the damage.

TOWER Insurance submits that it is more in keeping with the purposes of the new Act and continuing to drive alignment with the insurance industry, if the new Act were to provide that EQC must settle at the cost to replace or repair at the time of settlement. The fairness of this is especially apparent in cases where the circumstances of the natural disaster are such that widespread damage causes significant demand-surge inflation on reinstatement costs and services or where EQC has unreasonably delayed settling the claim.

This would simply mean a reversal of the current drafting in the Act so that the status quo is that EQC is obliged to settle based on what it would cost to reinstate at the time of the settlement of the claim with a discretion to not do this where, for example, a homeowner has delayed or unreasonably obstructed assessment and settlement of a claim.

TOWER Insurance favours settlement on the basis of cost to reinstate at the time of final settlement as this will be closest to the time when actual payment is made, minimises potential unfairness and accurately reflects the actual loss and the indemnity required. This approach also accords with private insurance practise and strengthens the alignment sought by these proposals.

A.6 EQC’s Salvage Rights

EQC has far-reaching salvage rights that enable it to take ownership of any property damaged by a natural disaster, and sell or dispose of the property until the insured advises in writing that they make no claim or if a claim is made, until the claim is withdrawn. If the insured hinders or obstructs the EQC in exercising its rights a claim can be declined and no liability attaches to EQC.

TOWER Insurance objects to the current Act as its sweeping powers not only impact harshly on the insured person, but also put at risks the rights private insurers have to salvage due to the limits of EQC’s cover. Salvage should be based on being exercised fairly and reasonably to protect the rights of the insurer or EQC. Further, salvage rights should be exercised in such a way that if the EQC insurance is exceeded, then the private insurers’ losses would be recovered first from any salvage. This is only logical as once the EQC cap is reached the repair/rebuild is the insurers’ responsibility and EQC simply pays the insurer its obligation.

A.7 Redefining volcanic eruption as volcanic activity more broadly

TOWER Insurance is not aware of the proposed extension of cover that is contemplated, but in principle would support a definition of this natural peril that is more comprehensive as this would minimise disputes around EQC cover. Further, and more importantly it would be important for both EQC and insurers’ cover to align. More information on this would assist us prior to the introduction of legislation.

A.8 Disclosure of information

Section 32(4) of the current EQC Act states that:

A person authorised by the Commission for the purposes of subsection (1) shall not make a record of, divulge, or communicate to any person, any information acquired in exercising the powers conferred by that subsection except—

- (a) to the Commission; or
- (b) for the purposes of this Act; or
- (c) for the purposes of any court proceedings; or
- (d) for such purposes as may be specified in any other Act.

This clause limits the sharing of information with insurers and it is not absolutely clear that if an insurer were acting on EQC's behalf with respect to an under cap claim that information could be freely shared to facilitate the recovery response.

TOWER Insurance seeks certainty from the Act to enable information that is gathered for the purpose of settling a claim to be shared between EQC and insurers.

A.10 Transitional arrangements

There are a number of issues TOWER Insurance submits should be addressed in the transition to a revised EQC scheme:

- Changes to the EQC Act and the proposed changes to the Fire Service Levy should both be aligned with respect to the attachment to fire policies for residential policies and ideally at the same sum. This would minimise transition costs.
- The timeframe for implementation should be at least 12 months. This reflects that insurers will be required to make two system changes (Fire Service Levy and EQC Levy) and that insurers typically send renewal notices to customer about two months in advance of the renewal date.
- The impact on private insurers' reinsurance arrangements. These arrangements will differ from insurer to insurer and will not necessarily coincide with EQC's reinsurance arrangements. These arrangements typically run year-on-year, so consideration needs to be given to a phase-in of these changes over a 12 month period.

It will also take some time for GNS Scientists and earthquake tool modellers (RMS / AIR etc) to understand any EQC changes and for this to flow through to risk modelling of insurance companies' expected loss from a modelled event. These matters have important implications for insurers' capital adequacy and reinsurance arrangements.

A minimum of 12 months would be needed to make necessary changes to systems and policies to implement the changes. Further, time would also be needed to ensure the necessary commercial arrangements are in place and agreed with EQC to enable insurers to handle under cap claims. This must be completed prior to the Act coming into force.

A.11 Election to reinstate/over-cap claims

Unless private insurers take over handling claims (in which case this issue falls away) it is submitted that EQC should not have the ability to elect to reinstate damage if a claim is over-cap. Once one event goes over-cap the entire reinstatement project should fall to the insurer. This would alleviate duplication of efforts between insurers and EQC and their contractors and provides certainty for a home owner as to who will be responsible for assisting them with their reinstatement.

A.12 Temporary accommodation, removal and storage of contents during under-cap reinstatements

Through the experience of the Canterbury earthquake sequence it became apparent that EQC's view was that it was entitled to refuse to pay the cost of removing and storing contents and relocation and accommodation costs of owners needing to move out while under-cap reinstatement work was carried out by EQC.

Eventually this matter was resolved with EQC accepting liability for these costs provided that there was no cross-over (i.e double-insurance) with private insurance entitlements. While a pragmatic resolution was eventually reached on this issue, it would be preferable for this to be clarified in the legislation.

It is our view that the costs of removing and storing contents to enable repair work to be carried out falls within the statutory cover provided by EQC under the current Act and that this should continue. Where EQC's contractors form the view that the removal and storage of contents and alternative accommodation of people living within the home is necessary to enable the repair work to be carried out, then it is TOWER Insurance's view that these costs are "reasonably incurred in respect of ... replacing or reinstating the building." Alternatively, those costs could be captured by subsection (iv) above.

-