

REFORMING THE EARTHQUAKE COMMISSION

Labour has already announced a package of measures designed to kick-start Canterbury's recovery – see <http://www.ownourfuture.co.nz/canterbury>. But there is more to be done. Drawing on the experience of Cantabrians, Labour wants to make sure the Earthquake Commission is properly structured and resourced to meet the needs of New Zealanders should we experience similar disasters in the future.

Summary

The Earthquake Commission (EQC) largely worked as intended after the devastating Canterbury earthquakes, despite being severely tested by the scale of the disasters. But with the Natural Disaster Fund now depleted and many lessons learned from the events in question, Labour believes it is necessary to review and reform several aspects of the EQC to ensure it is effective in responding to future disasters.

In summary, Labour will:

- Ensure Widespread EQC Coverage:

Labour will make EQC coverage universal by collecting levies through the local authority rates system.

- Increase the Cap on EQC Cover:

Labour will increase the \$100,000 cap on the EQC's liability – the new cap will be determined in consultation with the EQC and the insurance sector.

- Make the Levy Proportionate:

Labour will investigate altering the EQC levy to make it progressive, rather than a flat rate.

- Cover Temporary Accommodation Expenses:

Labour will expand the insurance coverage of the Earthquake Commission to ensure that temporary accommodation assistance is covered when private insurance expires.

- Review the Operations of Earthquake Commission:

Labour will review the structure and operation of EQC to ensure the lessons of the Canterbury earthquake are used to secure the long-term reliability of the Commission.

Ensure Widespread EQC Coverage

Labour will make EQC coverage universal by collecting levies through the local authority rates system and update the rules on land cover.

If a homeowner has private home insurance, then they also have EQC cover. Private insurance companies collect the levy for the government via its premiums. As such, EQC coverage is not universal. When uninsured properties are damaged in an earthquake or other natural disaster they are not eligible for an EQC payout and, in the case of Canterbury, uninsured homeowners were excluded from the Government's offer to buy red zone properties.

Making the EQC levy compulsory for homeowners via the rates system would eliminate the 'moral hazard' faced by the government when there are a substantial number of under- or uninsured homeowners with large repair bills after a natural disaster.

In Canterbury there was a backlash to suggestions that the government might provide assistance to those not covered by EQC after failing to take out private insurance. Such assistance for the uninsured is viewed as unfair by those homeowners who have prudently paid their insurance premiums to ensure they are covered.

Neither the Insurance Council nor the Earthquake Commission hold robust figures on the proportion of households without home insurance, but in Canterbury there were an estimate 10,000 houses under- or uninsured prior to last September's earthquake.¹

Collecting the levy through local authority rates would also provide the EQC with revenue for repairing land. Currently EQC receives no premium for its coverage of land (as opposed to buildings), but the escalating value of residential land in recent years has resulted in much higher payouts. Collecting the levy through rates would allow the EQC to meet the rising cost of repairing damaged land.

Some elements of the EQC's land insurance are unfair. The size of a claim can be influenced by a house's proximity to the section boundary, or whether it is a bungalow or multi-storey (i.e. the latter occupies less ground area). Variations in district plans can also affect entitlements. The coverage of damage to access ways is limited to 60 metres and this discriminates against rural homeowners. These aspects of the EQC insurance scheme will receive attention from Labour's review.

A compulsory EQC levy can be added easily to quarterly rates bills without burdensome compliance costs given the system is already established. Labour will work with councils to make sure that this change does not result in additional administrative costs.

The benefits of a compulsory, universal levy are clear: when New Zealand faces large-scale disasters, all of those affected will have guaranteed EQC cover. A rates-based system is fair and simple, clearing the way for swift and efficient recoveries in the future.

¹ 'Quake-hit uninsured may get govt bailout', 3 News website, 7 September 2010:
<http://www.3news.co.nz/Quake-hit-uninsured-may-get-govt-bailout/tabid/423/articleID/174692/Default.aspx>

Increase the Cap on EQC Cover

Labour will increase the \$100,000 cap on the EQC's liability – the new cap will be determined in consultation with the EQC and the insurance sector.

The EQC derives its income from a levy paid through insurance companies. The levy is based on the value of a home and its contents: 5 cents per \$100 for the first \$100,000 value of a home plus \$20,000 of contents up to a maximum of \$69 per year including GST. The EQC will cover up to \$100,000 worth of damage to an insured home in an earthquake, as well as \$20,000 of damage to contents.

National has announced that it intends to increase the levy to 15 cents per \$100 of insurance cover, meaning the maximum annual payment will be \$207. The increased levy is designed to speed the recapitalisation of the EQC's Natural Disaster Fund. The caps of \$100,000 and \$20,000 for coverage of damage to home and contents respectively would be retained by National.

The \$100,000 cap on home damage was set in 1993 based on construction costs from that time. The EQC advised the incoming National Government in 2008 that the cap should be doubled to \$200,000 in order to meet the cost of construction, which has greatly increased since 1993. A claim of \$30,000 in 1993 amounts to \$60,000 in today's money.

Further, EQC's exposure to payments for land damage has greatly increased in recent years: in 2003 the estimated value of all land under the EQC was \$65.6 billion; this trebled to \$207.6 billion in 2007. Yet over this period the EQC's premium income rose by just 9.25%.

We are aware that raising the EQC's cap will commensurately reduce the level of risk to which private insurance companies are exposed. Given some of the disaster risk will be transferred from the private market to EQC, we would expect insurance companies to lower their premiums accordingly.

Labour will, in setting the new cap, require that the newly created Insurance Commissioner negotiates with insurance companies to make sure that private premiums are reasonable and reflect the Crown's taking on of more risk from natural disasters.

Make the Levy Proportionate

Labour will investigate altering the EQC levy to make it progressive, rather than a flat rate.

More valuable properties are likely to incur more expensive damage in an earthquake than less valuable properties. Owners of more expensive homes, therefore, are likely to receive greater payouts than owners of less expensive homes, despite all homeowners paying the same flat-rate EQC levy.

Making the levy proportionate to the value of the property would be more progressive. Homeowners with more expensive properties would pay a greater proportion of the levy.

Cover Temporary Accommodation Expenses

Labour will expand the insurance coverage of the Earthquake Commission to include temporary accommodation assistance.

Standard home insurance policies generally cover much of the cost incurred by claimants when they are forced from their damaged homes as a result of an insured disaster. A range of expenses are covered including hotel bills.

However, insurance policies for temporary accommodation expenses are usually finite – as many Cantabrians discovered to their detriment. As we saw in Canterbury, large-scale disasters can leave people homeless for many weeks or months.

Undoubtedly, the Government has a responsibility to assist displaced people who are not covered by temporary accommodation assistance. The National Government was slow to respond when Cantabrians' private temporary accommodation expired, creating uncertainty at a difficult time.

Expanding EQC cover to include temporary accommodation expenses won't mean that private insurers stop being required to provide cover. Rather, the EQC cover would kick in once any private cover has expired.

Labour has previously announced that it would establish an independent Insurance Commissioner, who will design a plain-English household insurance "template" which includes certain minimum provisions such as temporary accommodation assistance.

Review the Operations of Earthquake Commission

Labour will review the structure and operation of EQC to ensure the lessons of the Canterbury earthquake are used to secure the Commission's long-term reliability.

The Canterbury earthquakes have exposed a number of issues and problems with the operation and structure of EQC, including:

- Complicated claims processes
- Confusion arising from claimants dealing with more than one agent (EQC and a private insurer)
- Delayed payouts to contractors from EQC, as well as confusion among claimants about the conditions attached to payouts
- Unreasonableness of the three-month time limit for the notification of EQC claims, and
- Complicated 'excess' policy that hasn't been updated since 1993.

As a result of the issues outlined above, Labour will initiate an extensive review of the Earthquake Commission's operations. The review will look at the EQC's assessment and triage process, considering whether there is alignment with the processes of private insurers. Looking forward, we will attempt to minimise the number of assessments required after a disaster to ensure quick payouts for victims, as well as ensuring the EQC can promptly access trained assessors.

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The EQC's internal processes will also be subject to review, including the billing and payments process. Labour is committed to ensuring households and contractors undertaking repair work have prompt access to funds in order to speed the recovery process after a disaster has occurred.

As part of the review, Labour would also consider the existing EQC excess policy in light of the Canterbury earthquakes and assess whether changes need to be made.

The EQC cannot accept claims more than three months after the insured event – and this is another aspect that Labour will review. The EQC has said there is “no good reason” for the limit, and it could be extended to one or two years.²

² Briefing to the Incoming Minister, Earthquake Commission, 2008