



11 September 2015

Review of EQC Act
The Treasury
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By email: Eqcreview@treasury.govt.nz

Proposed changes to the Earthquake Commission Act 1993: consultation

1. The New Zealand Law Society (Law Society) welcomes the opportunity to comment on the discussion document *New Zealand's Future Natural Disaster Insurance Scheme: Proposed Changes to the Earthquake Commission Act 1993* (discussion document). Our comments are brief at this stage, recognising that this discussion document is part of the negotiations to apportion risk between private insurers and the Government.
2. The Law Society acknowledges the significant work carried out by private insurers and the Government to produce this document. We look forward to working with all parties to ensure that the changes in legislation that result from this process provide the best solution to all New Zealanders.

Negotiations with private insurers

3. The Law Society recommends that consideration be given to the use of Memoranda of Understanding and other non-legislative provisions that could allow for flexible, pragmatic solutions.

Thematic issues

4. The proposals give rise to the following thematic issues:
 - a. No provision is made for uninsured householders. This issue requires reconciliation of the moral hazard inherent in providing EQC cover to people who choose not to buy insurance, and making sufficient provision to support communities in the event of natural disaster.
 - b. Conflicts will arise with outsourcing claims by private insurers and measures will need to be put in place to address these conflicts.
 - c. In any model where EQC and private insurers provide different cover there is potential for significant delays and litigation. In the proposed model, this is still an issue for land cover.
 - d. There are clear policy reasons for retaining a separate Natural Disaster Fund. The Law Society suggests that further cost/benefit analysis be undertaken and input obtained from industry participants.
5. The Law Society identifies a number of options below in respect of each issue (without expressing a view on them), for the purpose of ensuring all possible solutions have been identified and considered.

Uninsured householders

- a. Making a certain minimal level of insurance cover compulsory for householders.
- b. Requiring EQC to contact those homeowners whose properties are uninsured annually, to offer minimum cover under section 22 of the EQC Act.
- c. Setting up a discretionary mutual fund that can meet the needs of uninsured householders in the event of a disaster. A discretionary mutual fund could have the advantage of international reinsurance rates without the moral hazard of guaranteeing payments to households who chose not to insure.

Conflicts in outsourcing

- d. Creating mechanisms to reduce the inherent conflicts in private insurers managing claims. Consideration could be given to whether the conflicts would be reduced if a mechanism were created to allow the Government to provide a 50 per cent quota share reinsurance of the first \$400,000 of any loss rather than accepting the first \$200,000 of every loss. Providing quota share reinsurance would also ensure that the Government's coverage matched the insurance coverage, so avoiding many of the complexities and possible arbitrage opportunities available with providing two different layers of insurance cover.

Mismatch between EQC/private insurers land cover

- e. Requiring private insurers to provide back to back insurance cover for land with the Government, but the Government reinsuring the private insurer's liability.
 - f. Alternatively, no land cover is provided by EQC or private insurers, but the Government sets up a discretionary mutual fund (such as described in 5(c) above) which is used to remedy damage to land in circumstances set out in the proposal 9 on page 30 of the discussion document.
6. The insurance industry has not yet been subject to significant digital disruption. It is anticipated that this disruption will occur and that the traditional methods of placing insurance and apportioning risk between insurers, reinsurers and the capital markets will continue to change and develop. For this reason it is important that the legislation is drafted to allow it to operate with flexibility.
 7. The proposal to allow EQC to use alternative risk transfer mechanisms and for the legislation to enable the regular reviews of monetary settings and caps (as envisaged) but also of the subject matter of the insurance, is in a similar vein. With changes in the international insurance and reinsurance industry, it may be that some types of catastrophe cover become unavailable and EQC should be provided with flexibility to meet both changing needs and changing responses by international benchmarks.
 8. The new legislation should be future-proofed so far as possible so that such core concepts as "residential" are sufficiently flexible to be able to deal with society's changing needs. Already there is a breakdown in the lines of demarcation between work and home, because of the increasing numbers of people who work remotely or own their own business.

Technical issues

9. The discussion document indicates that an amended EQC Act will include a number of technical changes. These changes are signalled, but not discussed, in the discussion document. Whilst a number of these technical issues will, of necessity, result from the policy decisions that affect the future role of EQC and the inter-relationship between EQC as provider of catastrophe cover and private insurers, further consideration of the following would be welcomed:

- a. a review of the circumstances in which EQC may pay claims to people other than the insured person (typically a mortgagee) with insurable interests in the damaged property;
- b. the requirements for the assignment of claims and settlement with the assignee; and
- c. addressing the Canterbury Earthquakes Royal Commission recommendation 94, to amend section 32(4) of the EQC Act to allow for disclosure of information that may affect personal safety.

Conclusion

10. This submission has been prepared by the Law Society's Commercial and Business Law Committee. If further discussion would assist, the committee convenor Rebecca Sellers can be contacted through the committee secretary Karen Yates (ph 04 463 2962, karen.yates@lawsociety.org.nz).

Yours sincerely,

A handwritten signature in black ink, consisting of a stylized initial 'C' followed by a long horizontal line.

Chris Moore
President