

New Zealand High Court rules on Earthquake Commission's reinstatement argument

Earthquake Commission HCWN CIV-2011-485-1137

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Background

New Zealand's Earthquake Commission (EQC) is a government agency which was established to operate as an effective 'first layer' of insurance cover where a residential homeowner has full replacement value cover under an insurance policy.

The EQC covers the replacement value of the property to a maximum of (generally) NZ\$100,000 (plus a further NZ\$20,000 for personal property) in the event of an earthquake recognised by the EQC as sufficiently powerful to cause natural disaster damage covered under the Earthquake Commission Act 1993 (the Act). It is understood that the EQC is protected by reinsurance of NZ\$2.5bn with an excess of NZ\$1.5bn (with one free reinstatement).

Since September 2010, there have been no fewer than 13 earthquakes which the EQC has recognised as giving rise to natural disaster damage. Of these, the largest two took place on 4 September 2010 and 22 February 2011, and the great majority of claims received by the EQC arise from these two quakes (and are divided almost equally between the two).

Issue in dispute

The New Zealand High Court had been asked to resolve the issue of how the EQC cover responds to homeowners who have made more than one claim for damage, suffered in more than one earthquake, where such damage exceeds, in aggregate, NZ\$100,000 (or NZ\$20,000). If, at the time of the subsequent earthquake, the EQC has not yet paid in respect of the first earthquake, is it liable to pay up to NZ\$100,000 in respect of each earthquake or no more than NZ\$100,000 in total, until cover is reinstated by, for example, payment of a claim?

A key provision in the Act is clause 6 of Schedule 3. This provides (in relevant part) that:

on the payment by [the EQC] of any amount for any natural disaster damage to any property, *the insurance under this Act shall continue to the same extent as before the natural disaster damage occurred* but [the EQC] shall be entitled to charge the insured person...for the continuation of the insurance an amount calculated in accordance with regulations made under this Act (emphasis added).

The EQC sought to argue that the Act provided insurance to an aggregate amount of NZ\$100,000 only for all natural disaster damage occurring during the period of insurance. The amount of insurance is reinstated to NZ\$100,000 for any further earthquake occurring after the date of renewal of the insurance policy or payment for the first earthquake (whichever is earlier).

That argument was rejected by the High Court (sitting in full bench). Nothing in the Act suggested that cover is to be reduced when damage occurs or a claim is made. Instead, while an insurance policy is in force, property remains insured for damage resulting from a second earthquake.

As to the meaning of 'on the payment' by the EQC as set out in clause 6, the High Court found that this was an:

adverbial phrase, signifying that it is the act of payment which triggers the operation of clause 6. They mean 'in the event of payment' rather than 'with effect from the date of payment'. That being so, they do not limit clause 6 to the time subsequent to the date of payment.

A further issue was then considered. Is it the case that cover for the second earthquake is reduced by the amount payable on the claim for the first earthquake but then reinstated to NZ\$100,000 on the payment by the EQC of any amount in respect of the first earthquake (that reinstatement retrospectively taking effect from the date of the first damage or the date the claim for the first damage was made)? The High Court found that payment of a claim triggers clause 6 but that it makes no difference whether the natural disaster damage occurred before or after that triggering event.

Accordingly, the Act provides for continuing cover and neither the occurrence of (nor the making of a claim for) an event of natural disaster damage reduces the amount of cover available for a subsequent event of natural disaster damage, at any time prior to, or on payment of, a claim for the first event.

It is not yet known whether the EQC intends to appeal this decision to the New Zealand Court of Appeal.

Comment

This decision, confirming that the Act provides for continuous cover and that reinstatement of cover does not depend on whether payment (in full or in part) has been made by the EQC, will be welcomed by London reinsurers of New Zealand property insurers. It represents, we would suggest, a commonsense and commercial approach to the interpretation of the Act. In particular, any suggestion that reinstatement might potentially depend on actual payment by the EQC of claims would be fraught with difficulties. In short, the EQC would have no incentive to pay claims quickly (and, in any event, a major loss would be expected to lead to a significant backlog in the adjustment and payment of claims).