MELVILLE JESSUP WEAVER
Towers Watson Alliance Partner

6 March 2014

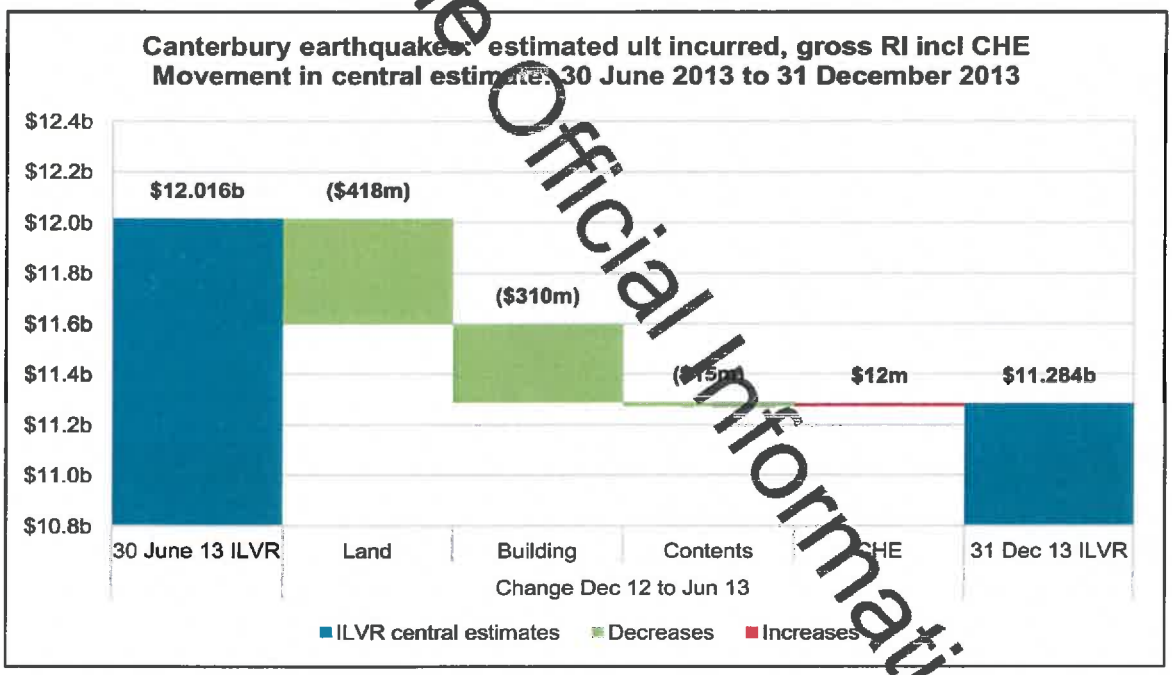
Mr Ian Simpson
Chief Executive Officer
Earthquake Commission
PO Box 790
WELLINGTON

Dear Ian

EQC – Movement in gross ultimate incurred claims costs: 30 June 2013 – 31 December 2013

I refer to the EQC Board meeting on 17 February 2014 where it was requested that we provide more detail on the movement in the gross ultimate incurred claims costs between 30 June 2013 and 31 December 2013.

The estimated ultimate gross claims cost has decreased from $12.016b as at 30 June 2013 to $11.284b as at 31 December 2013. A breakdown of this change is shown below.



Canterbury earthquakes only
Comparison to 30 June 2013 ILVR Results

	Dec 13 $m	Jun 13 $m	Change $m
Land	1,614	2,031	(418)
Building	7,965	8,275	(310)
Contents	456	472	(15)
Claims handling expenses (CHE)	1,250	1,238	12
Total	11,284	12,016	(731)

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Movement categories

For each of these liability movements we have attempted to break down the overall figure into *hard movements* and *soft movements*.

A hard movement is defined as one that is reasonably certain. This may be because the settlement process is under way or has a high degree of confidence of success.

A soft movement is defined as one that is less certain of its ultimate outcome. This may be because of possible legal challenges, because the process has not begun or has a lower degree of confidence of success.

Land

The estimated gross ultimate incurred claims cost in respect of land sub-claims has decreased from $2,031 million to $1,614 million, a decrease of $418 million. This decrease can be further sub-divided into the following causes:

- -$222 million. Category 1 – 7 damage categories have a lower estimated cost to repair. As this is visible damage and the repair process is well known, this is a hard movement.
- $55 million. Category 8 vacant land repair costs. The estimated costs to repair Category 8 damage for vacant sections have been updated. While this is not visible damage, there is much greater certainty on the likely costs of repair. Consequently this is considered a hard movement.
- -$74 million. Buildings moving from repair to rebuild. As at 30 June 2013 it was assumed that the Category 8 and 9 repair costs were for vacant land. Clearly, enabling works would only be required for repairable buildings. Between June 2013 and December 2013, some of these repairable properties were re-classified as rebuilds, reducing the amount of enabling works. This is a hard movement.
- $120 million. Eligibility for Category 8 and Category 9 remediation. EQC have refined their criteria for eligibility to remediate Category 8 and 9 land damage. This has resulted in a greater number of properties qualifying for remediation. This is a hard movement.
- -$37 million. Port Hills. The estimated costs to repair land in the Port Hills has decreased. These claims have largely been settled. This is a hard movement.
- $55 million. Other hard movements. This includes changes to inflation, demand surge, unclaimed damage, silt removal and the impacts of the EQC excess. These are all considered hard movements.
- 9(2)(e) Enabling works. Due to the EQC sponsored land trials, remediation strategies which do not require a vacant section (and hence enabling works) are possible. This has not been operationalized so is considered a soft movement.
- 9(2)(e) Repair costs: non-vacant vs vacant. The land repair costs for a section with a building on it are higher than for vacant land. This leads to higher costs where the building is a repair. This is the flip side of enabling works and is therefore a soft movement.
- -$102 million. Category 9 DoV. It is intended that Category 9 damage will be cash settled by reference to diminution of value of the property. This has yet to be operationalised and so is a soft movement.

The hard movements above have been determined by starting with the position as at 30 June 2013 and estimating the changes that would occur using the information as at 31 December 2013.

The remaining movements relate to changes in the way in which Category 8 and Category 9 damage may be remediated. These are taken to be soft movements. The split of the soft movement between the three causes should be taken as approximate only.

Appendix A contains a summary of these movements.

Building

The estimated gross ultimate incurred claims cost in respect of building sub-claims has decreased from $8,275 million to $7,965 million. This decrease can be further sub-divided into the following causes:

- -$285 million. GST adjustment. The ACE model previously used input data that was incorrectly assumed to be GST exclusive. This is considered a hard movement.
- -$114 million. EQR data - settled. The valuation as at 31 December 2013 utilises considerably more settled data than as at 30 June 2013. These settled claims have lower costs than previously predicted and this has led to a lower estimate of ultimate claims costs. This is a hard movement.
- -$6 million. Refined approach. The valuation as at 31 December 2013 utilises more data and in a slightly different manner to predict how open claims eventually settle. This has resulted in a slightly lower estimate of ultimate claims costs. This is a hard movement.
- $154 million. Demand surge. This has been strengthened on the basis of more information from building / labour indices, the EQC executive and industry news. This is a hard movement.

Appendix A contains a summary of these movements.

Other

The estimated gross ultimate incurred claims costs in respect of contents sub-claims and CHE have remained relatively static and for the purposes of this analysis, we have taken the combined movement (-$3 million) as being a hard movement.

Summary

The gross ultimate incurred claims cost has reduced by $731 million over the six month period to 31 December 2013. This can be broken down into hard and soft movements as shown below.

Gross ultimate incurred claims costs

	$000	$000
30 June 2013		12,015,538
Hard movements		
Land	(101,757)	
Building	(310,032)	
Contents	(15,305)	
CHE	11,720	
Total	(415,374)	
Sub-total		11,600,164
Soft movements		
Land	(315,992)	
Overall	(731,366)	
31 December 2013		11,284,172

Yours sincerely

Craig Lough

Fellow of the NZ Society of Actuaries

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A Summary of Land and Building movements

Land liability movements

Type	Movement $000
Hard	
Cat 1-7 damage	(221,642)
Cat 8 vacant land repair	55,312
Repair to rebuilt	(73,922)
Eligibility	120,454
Port Hills	(37,016)
Other items	55,056
Sub-total	(101,757)
Soft	
Enabling works	[redacted] 9(2)(e)
Cat 9 DoV	(102,269)
Non-vacant repair	[redacted] 9(2)(e)
Sub-total	(315,992)
Overall	(417,749)

Building liability movements

Type	Movement $000
Hard	
GST adjustment	(285,032)
EQR data solid movement	(173,757)
Demand surge	154,449
ACE model refined approach	(5,692)
Sub-total	(310,032)
Soft	
-	0
Overall	(310,032)