

Diminution of Value (DOV)

due to Increased Flooding Vulnerability (IFV) land damage (for where the house is still in place)

FACT SHEET – November 2016

What is Diminution of Value (DOV)?

DOV measures the reduction in a property's market value which has been caused by Increased Flooding Vulnerability (IFV) land damage.

When EQC cash settles (IFV land damage), it assesses the customer's loss in one of two ways - either:

- the amount it would cost the customer to repair the land damage (the repair cost); or
- DOV.

This fact sheet focuses on IFV settlements that are assessed solely on the basis of DOV.

Furthermore, it only deals with the situation where the house that was on the property before the 2010-2011 Canterbury earthquakes is still in place and is not to be rebuilt. In those cases, the DOV reflects the impact of the IFV damage on the insured land and the associated residential buildings, such as the house, garage and garden shed.

DOV does not measure the impact of an increase in flooding vulnerability caused by off-site effects, such as narrowing of river banks, shallower river beds and damage to storm water drains.

Why is EQC using DOV to settle some IFV land damage claims?

In many cases it is not possible to identify an appropriate repair for IFV land damage. For example, this may be because:

- it is not feasible to carry out a repair of the IFV land damage. This may be the case if the house has to be removed in order to do land repairs to address IFV damage under the house; or
- it is not possible to carry out the repair legally. For example, it may not be possible to get a resource consent required under the Resource Management Act for the land repairs to the IFV damage.

In these cases, EQC is not able to base the settlement on repair cost. Instead, EQC is basing the settlement of IFV land damage on the reduction in value of the property due to this land damage. This is called DOV.

The High Court has confirmed in its Declaratory Judgment in December 2014 that EQC can settle IFV land damage by paying the amount of the DOV in appropriate cases.

What approach do EQC's valuers take to assessing DOV where the house is still in place and is not to be rebuilt?

For this situation, EQC's valuers have developed a standardised approach to assessing whether increased vulnerability to flooding impacts on a property's market value. This approach is designed to ensure that DOV is assessed in a consistent way for IFV customers in this situation.

The methodology for determining DOV has been approved by a peer review panel of valuers. The panel members were nominated by the major New Zealand professional valuation associations.

How is DOV assessed where the house is still in place and is not to be rebuilt?

Once EQC's engineers identify a property as being more vulnerable to flooding under the engineering assessment, a registered valuer undertakes an initial assessment of the property.

If the initial assessment identifies no reduction in the property's market value (and the DOV is therefore nil), then the property will not qualify for IFV land damage. In this case, the valuer will not carry out further assessments.

However, if the registered valuer's initial assessment identifies a reduction in the property's market value, the valuer will take the following three steps to assess the amount of DOV for the property with IFV land damage:

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1) Establish the pre-earthquake value of the property

The valuers use recognised techniques to establish the value of the property as at 3 September 2010. To help determine this value, verifiable evidence has been gathered from a variety of sources. This evidence includes:

- information on the sales for the area; and
- building age and size.

The valuation is made as at 3 September 2010, the day before the first earthquake in the Canterbury earthquake sequence. This is to ensure that the valuation is a fair market valuation and is not distorted by the effects of the earthquakes on the property market.

2) Determine the amount of the reduction in the property's market value because it has IFV land damage

To assess the amount of the long-term market reduction of value, EQC's valuers take into account factors, such as:

- depth of the increased future flooding;
- location of that flooding (including in relation to any residential buildings), and its likely frequency; and

- features of a property that make it more or less likely to lose value due to a risk of flooding. For example, the location of the property and its views are often major drivers of valuation. The location and views may be such that the market could reasonably be expected to attach less weight to IFV damage to the property.

3) Exercise valuation judgement as to the resulting DOV

The valuer makes a final check to ensure the reduction in value determined for the property is appropriate as a matter of valuation judgement.

Every valuer's assessment of a property is reviewed by a senior valuer.

Can a property be identified by EQC's engineers as being more vulnerable to flooding, but EQC's valuers determine that the increased vulnerability has had no impact on the property's market value?

Yes. This may occur for example, where the likely location of the increased future flooding is only on a part of the insured land that is away from the house. Although that part of the insured land is more vulnerable to flooding, the valuer may determine that the increased vulnerability has not reduced the value of the property.



What if a customer whose land settlement for IFV was based on DOV, believes their land can be repaired?

If a customer can show that they can in fact obtain a resource consent for the land repair and that they will do the land repair, then the settlement amount may be changed to be based on repair cost. This is unless the repair cost is disproportionate to the amount of the DOV. This comparison will be determined on a case by case basis.

Where a property with IFV has been sold since the earthquakes, the settlement will also be based on the DOV. This settlement approach for IFV land damage is consistent with the Declaratory Judgment which was delivered in December 2014.

Settlement amounts are also subject to the land cover cap amount which is set out in section 19 of the Earthquake Commission Act (EQC Act). The EQC land cover cap is generally the value of the area of damaged land or the value of a parcel of land that is the minimum lot size under the relevant District Plan, whichever is the smaller.

Why is there no indexing of the DOV assessment to reflect the increase in property market valuations in general in the Christchurch market in the last five years?

When doing the DOV assessment, EQC starts by assessing the market value of the property immediately before the earthquakes (3 September 2010). EQC then

uses this value as the base for calculating the reduction in value (DOV) of the property that has occurred since that date as the direct result of the IFV damage caused by the earthquakes.

In accordance with the EQC Act, EQC assesses the base land value from the date immediately before the damage occurred. There is no scope under the EQC Act to choose a base value as at a future date (i.e. after the date of the damage), or somehow apply an index to increase the amount of the base value.

EQC has assessed the base valuation as at 3 September 2010 for all the earthquakes that have caused the IFV damage. This is to ensure that the base valuation is a fair market valuation and is not distorted by the effects of the earthquakes on the property market since 3 September 2010.

What do I have to do with the settlement amount assessed on the basis of DOV?

A DOV settlement amount is paid where there is no feasible repair available for the IFV land damage, or because the repair is not able to be done legally. While you may wish to use the settlement amount to mitigate the effects of any future flooding, there is no requirement to do so.

If you do not use the DOV settlement amount to repair the IFV damage, it will not affect future EQC cover for the property.

Depending on how much the settlement amount is, it may be paid to the mortgage provider of the property.

For more detail on DOV for IFV damage, see www.eqc.govt.nz/IFV