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EQC
EARTHQUAKE COMMISSION
Kōmihana Rūwhenua

STATEMENT OF PERFORMANCE EXPECTATIONS 2017-18

This Statement of Performance Expectations (SoPE) is a formal public accountability document required under section 149C of the Crown Entities Act 2004. It outlines the Earthquake Commission's (EQC's) planned work and financial information for the period 1 July 2017 to 30 June 2018. Relevant historical and forecast comparison information is also provided for the benefit of readers.

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Kōmihana Rūwhenua
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CONTACT

EQC: info@eqc.govt.nz
Phone: +64 4 978 6400
www.eqc.govt.nz

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STATEMENT OF RESPONSIBILITY

This Statement of Performance Expectations (SoPE) sets out EQC's intended non-financial performance and financial forecast for the year 1 July 2017 to 30 June 2018 across its Output Classes, and has been prepared in accordance with the Crown Entities Act 2004.

The prospective financial statements have been prepared in accordance with PBE FRS-42 for the purposes of this SoPE. The financial statements have not been audited and should not be relied upon for any other purposes. EQC is responsible for the preparation of this SoPE, including the forecast financial statements and the assumptions on which they are based, the non-financial measures and for the judgments used in preparing them.

Sir Maarten Wevers KNZM Board Chair 22 May 2017	Mary-Jane Daly Commissioner 22 May 2017

INTRODUCTION AND BACKGROUND

EQC's functions are set out in section 5 of the Earthquake Commission Act 1993 ("the Act"). Those functions are:

a. *To administer the insurance against natural disaster damage provided under this Act:*

b. *To collect premiums payable for the insurance provided under this Act:*

c. *To administer the Fund and, so far as is reasonably practicable, protect its value, including by the investment of money held in the Fund:*

d. *To obtain reinsurance in respect of the whole or part of the insurance provided under this Act:*

e. *To facilitate research and education about matters relevant to natural disaster damage, methods of reducing or preventing natural disaster damage, and the insurance provided under this Act:*

f. *Such other functions as may be conferred on it by –*

   i. *This Act or any other Act; or*

   ii. *The Minister, in accordance with section 112 of the Crown Entities Act 2004.*

EQC's Statement of Intent (SOI), contains the strategic objectives and operating priorities that give effect to the functions in the Act and, guide the delivery of EQC's services (or outputs). This SoPE has been drafted to align with this strategic direction and should therefore be read in conjunction with EQC's SOI for 2014-18. The actual performance for the 2017-18 financial year in each of the outputs and measures in this SoPE will be reported in EQC's Annual Report for that year.

EQC's strategic objectives are:

- New Zealanders have access to natural hazard insurance and reinsurance;
- Claims made to EQC's insurance scheme are managed fairly, transparently and in a timely way; and
- EQC is a leader in New Zealand on natural hazard risk reduction, delivering improved national resilience to natural hazards.

Supporting these objectives are Four Key Result Areas (KRA's) that EQC will focus on EQC's priorities and operations. The outputs in this SoPE are a key means by which EQC both progresses its KRA's, priorities and operating activity and, discharges the functions in the Act. The outputs in this SoPE are grouped into four categories (or output classes):

1. Administration of the EQC Act, Insurance Scheme and Natural Disaster Fund (together, "Administration");
2. Customer Services;
3. Research; and
4. Education.

For each of the above output classes this SoPE provides information on:

- Objectives and measures;
- The expected revenue and proposed expenses; and
- How the performance will be assessed.

The SoPE also provides EQC's prospective (forecast) financial statements for the 2017-18 Financial year.

Figure one shows the alignment of the SoPE output classes (that contain the detailed measures) with the KRA's in EQC's strategic direction.

OUR OPERATING CONTEXT

EQC's Vision, Mission and three Strategic Objectives provide the overarching framework for its work while meeting its obligations under the Act. It is important to note that while EQC's delivery aligns the Act's broad strategic context and the annual output classes delivery, there is a Review of the Act underway that could influence the structure and content of future accountability documents. The review is being undertaken by Treasury and any changes will be considered once the review is complete.

In this SoPE, EQC has included Output Class measures and targets to deliver on its revised medium-term Key Result Areas, which contain the goals and priorities for EQC. With the appointment of a new Chief Executive, Sid Miller, and following the Kaikoura earthquake 2016, the Key Result Areas have been refined to:

- EQC is a leader for a risk aware New Zealand;
- EQC underpins an effective insurance market in New Zealand;
- Event Management; and,
- EQC has an operating model that makes us easy to do business with.

The first two Key Result Areas are unchanged from 2016-17. EQC's work to improve New Zealand's risk awareness and reinsurance remains vitally important. Building on the work it has already done, EQC is developing a Natural Disaster Risk Strategy to be ready by the end of 2017. This strategy will pull together work already underway across a number of areas including both research and public education and reflects the leadership role that EQC plays in ensuring New Zealand and New Zealanders have high awareness of natural hazard risks.

Work is underway to develop a Risk Financing Strategy to clarify reinsurance principles and rebuild the Natural Disaster Fund.

The third Key Result Area, Event Management, covers the work EQC is doing in response to the numerous natural hazard events which occurred in recent years, and the earthquakes, floods, landslips, hydro thermal events or tsunamis that may occur in the future. The Canterbury and Kaikoura earthquakes are the largest events in terms of claims lodged. EQC maintains readiness to respond to events in different ways, and adapts delivery as we learn what works well. For example, most of the claims following the Kaikoura earthquakes are being managed by the insurers acting as EQC's agents.

The final Key Result Area is ensuring EQC has an operating model that makes us easy to do business with and has customer experience at its core. This work will build on the initiatives and changes made in recent years to our operating model and will incorporate learnings from previous event responses.

While much of the work that supports these Key Result Areas spans timeframes beyond the SoPE, the Key Result Areas provide the linkage between EQC's strategic objectives and output class delivery. While the output classes themselves are measures specific to our reporting framework, they reflect the ongoing work of EQC.

Highlights of this work

Estimated premium revenue of **$281 MILLION** to end of the 2016-2017 financial year

Since the beginning of the 2010/11 Canterbury earthquakes EQC has set up the Canterbury Home Repair programme which has completed over **67,000 HOME REPAIRS**

In the 2016-17 financial year to date, the contact centre has answered over **2,430** inbound calls and **877** emails on average **PER WEEK**

Figure One: EQC Reporting Framework 2017-18

VISION: TO BE THE WORLD'S LEADING NATIONAL NATURAL HAZARD INSURANCE SCHEME

MISSION: TO REDUCE THE IMPACT ON PEOPLE AND PROPERTY WHEN NATURAL DISASTERS OCCUR

STRATEGIC OBJECTIVES

- New Zealanders have access to natural hazard insurance and reinsurance
- Claims made to EQC's insurance scheme are managed fairly, transparently and in a timely manner
- EQC is a leader in New Zealand on natural hazard risk reduction, delivering improved national resilience to natural hazards

KEY RESULT AREAS

- Event Management
- EQC has an operating model that makes us easy to do business with
- EQC is a leader for a risk aware New Zealand
- EQC underpins an efficient insurance market in NZ

OUTPUT CLASSES

- Administration
- Customer Services
- Research
- Education

SOPE REPORTING

EQC INPUTS: People, Processes, Systems, Machinery of Government, Risk Management

EQC has resolved
99.5%
of claims from the 2016 Valentine's Day earthquake in Canterbury

Provided funding of
$12.3 MILLION
to GeoNet in the 2016-2017 financial year

In the first five months since the November 2016 Kaikoura earthquake, EQC has paid out
$15.6 MILLION
to customers

PART 1: OUTPUT CLASSES

Output One: Administration

The Administration Output class covers EQC's activities and services for:

- the administration of the Natural Disaster Fund (the Fund) – including collection of the premiums payable;
- the investment of money held in the Fund; and
- obtaining reinsurance in respect of the whole or part of the insurance provided under the Act.

The Fund is the fund from which EQC pays settlement amounts for claims for physical loss or damage from specified natural disaster events. The assets in the Fund are invested and along with a reinsurance programme are intended to meet any EQC future natural disaster insurance liabilities. The Government provides EQC (under section 16 of the Act) with a guarantee of EQC's liabilities. This guarantee recognises that financial resilience for natural hazard risk contributes directly to ensuring that New Zealanders have access to natural hazard insurance and reinsurance.

EQC's performance in other outputs also contributes to the administration of the EQC insurance scheme and the Fund. For example, obtaining adequate and affordable reinsurance is supported by the transparent and good faith representation of New Zealand's potential risk of physical loss or damage to residential property from natural disasters. The natural hazard disaster research activities for Output three contribute to the understanding and assessment of this risk.

Output objectives

The objectives for this output are to:

- Administer the Fund by:
  - investing the fund conservatively and maintaining its liquidity to meet claims in the aftermath of the Canterbury earthquake sequence and 2016 Kaikoura earthquake;
  - ensuring that premiums payable under the Act are collected in accordance with the Act; and
  - obtaining appropriate reinsurance cover.[1]

How we measure performance

The return on the Fund is measured against the NZX 90 day bank bill rate with financial reports on progress provided monthly to the Board and on a quarterly basis to Treasury.

We also monitor performance in the Output Class by ensuring reinsurance costs align to parameters agreed by the Board. This is reported to the Board and Treasury on a monthly basis.

Expected revenue and proposed expenses

Expected revenue from EQC premiums for Output one is $285.9 million. Proposed expenses for Output one are $174.1 million. Expenses include $10 million payable to the Crown for the Crown Guarantee, with $164.1 million available to purchase reinsurance.

1 An estimated 98 per cent of New Zealand's residential property owners currently have EQC insurance cover, as they are the holders of private residential building and/or contents contracts of insurance with cover for fire.

Performance measures

Table One: Output One Performance Measures and Targets 2017-18

OUTPUTS	MEASURES	TARGETS 2017-18
Invest in, and Administer the Natural Disaster Fund	■ Annual investment portfolio performance in relation to 90 day bank bill rate ■ Premiums collected meet the Board agreed budget ■ Fund Administration is completed in accordance with the SIPSP and Ministerial Direction	■ Average rate of return exceeds NZX 90 day bank bill rate less 25 basis points (per annum) ■ Quarterly premium collection meets budget amount +/- 2.5% of forecast ■ 100% SIPSP objectives[2] are met ■ 100% SIPSP variations are duly authorised
Obtaining reinsurance	■ Subject to market conditions EQC obtains reinsurance consistent with budget policy and range set by the Board	■ Cost of reinsurance programme is within the budget set by the Board[3] ■ Nationwide coverage obtained for all natural disaster perils covered under the EQC Act

2 The SIPSP Objectives are at: http://www.eqc.govt.nz/about-eqc/our-role/sipsp
3 The Board has accepted reinsurance cost variables that provides a minor increase to the agreed 2017-18 budget

Output Two: Customer Services

The Customer Services output class covers EQC's activities for the settlement of claims for natural disaster damage through the EQC insurance scheme.

The number of claims for damage handled by EQC can vary each year from a few thousand to hundreds of thousands. Both the efficiency of our claims handling systems and processes coupled with the manner in which customer claims are handled by EQC have a significant impact on customers' experience and perception of EQC and its service. EQC customers expect a fair, transparent and timely settlement of their claims. Premium payers and reinsurers expect us to manage our business cost-effectively and with appropriate transparency.

Completing the remaining Canterbury[4] activity and working with private insurers to progress Kaikoura[5] claims through a Memorandum of Understanding, are priorities "in this output for 2017-18. This includes:

- improving the customer experience and journey through the claims settlement process and customer communication;
- the safe repair of damaged residential properties;
- learning from engagement with the private insurers to improve future outcomes.

During 2017-18 we expect to resolve all workable[6] residual Canterbury claims and complete the Canterbury land settlement work, drainage work, and remedials recorded to February 2017. There will also be a significant amount of 'non-claims' work arising from Canterbury to complete (eg. working with insurers and re-insurers to determine final allocation of costs).

In the same timeframe we will also settle the majority[7] of approximately 38,000 Kaikoura claims across all claim areas – residential land, residential buildings, and contents.

Output objectives

The objectives for this output are to:

- calculate and resolve claims correctly, and according to the Act;
- progress all event claims within agreed targets;
- respond appropriately to customers and stakeholders; and
- complete EQC's Canterbury response (remedials, drainage, land), EQC's Kaikoura response working with private insurers (land, residential buildings, contents), and responses to a number of smaller events.

How we measure performance

The Customer Services Output Class results are tracked through claim information collection by Customer and Claims and through the Business Information Unit. Progress against targets is reported monthly to the Board and quarterly to Treasury as EQC's monitoring agent.

Expected revenue and proposed expenses

Output two has no expected revenue. Proposed expenses for Output two are $32.7 million[8] (subject to no new natural disaster events in the financial year).

4 Refers to the Canterbury 2010/11 Earthquake sequence
5 Refers to the 14 November 2016 earthquake and aftershocks
6 Workable: Includes all claims not in formal litigation that can be progressed by EQC as far as possible
7 Majority: EQC expects that all claims that can be settled, will be. The exceptions may relate to those where litigation is occurring, or where decisions are outside EQC influence.
8 Note the $32.7 million relates to EQC's base catastrophe response programme and claim handling expenses for smaller events.

Table Two: Output Two Performance Measures and Targets 2017-18

OUTPUTS	MEASURES	TARGETS 2017-18
Claims are settled in accordance with the EQC Act and other relevant legislation	■ Customers are paid within one year of the damage being duly determined in accordance with the Act	■ 100%
EQC is easy to do business with (claims handling)	■ All Events: Customer satisfaction[9] with the overall quality of service from EQC ■ All Events: Customers who report they were kept well informed throughout the claim settlement process	■ 60% of customers report satisfaction with the overall quality of service from EQC ■ 75% of customers consider that they were kept well informed throughout the claim settlement process
	■ Kaikoura: Positive customer satisfaction rating for the overall Kaikoura event	■ 75% of Customers are satisfied
Effective management of claims handling expenses	■ Financial performance for all events for which a Claims Handling Expense budget has been approved	■ Within 10% of the 2017-18 financial year Board approved budget for: – Canterbury – Kaikoura – All other events
Canterbury 2010 and 2011 earthquake remedial claims	■ Canterbury: All remedial[10] claims as at February 2017 are settled by 31 December 2017[11]	■ 100%
EQC maintains a safe working environment	■ A safety focused environment for the settlement of claims is implemented	■ No more than 5.5 injuries per million hours worked, with incidents closed within 10 days

9 Quarterly telephone survey conducted by external research for EQC comprising of 350 respondents from a randomly selected sample of about 1000 customers per month. The results are aggregated quarterly. "Satisfaction" means response of 4 or 5 to the question: "Using a 1-5 scale where 5 means very satisfied and 1 means very dissatisfied, how satisfied were you with the overall quality of service delivery from EQC?"
10 Including sub-floor repairs.
11 Note: There may be remedial claims raised and accepted during 2017-18 that may be received late in the period, thereby necessitating delivery in 2018-19

Output Three: Research

New Zealand is a geologically active country with a high exposure to natural disaster risk. EQC funded research and education contributes to improved understanding and management of natural disaster risk in New Zealand with a focus on risk reduction and resilience.

The research output class covers EQC's activities to facilitate research and education (collectively 'Research') about:

- matters relevant to natural disaster damage;
- methods of reducing or preventing natural disaster damage; and
- the insurance provided under the Act.

Output objectives

In relation to enhancing the understanding of natural disaster risk, including the reduction and prevention and insurance coverage of the perils in the Act, the objectives for this output are to:

- Fund high-quality and publicly available research and natural hazard information projects:
  - to create a current, integrated picture of natural disaster risks in New Zealand to inform natural hazard risk management and risk financing strategies
  - that support New Zealand innovation by investing in research capability and investigator-led research to encourage emerging talent and new ideas
  - that underpin knowledge base and fill information gaps about natural hazard risk reduction, risk financing, claims management and disaster recovery.
- Disseminate EQC funded and facilitated research and natural hazard information that:
  - improves collective understanding, promote collaboration and innovation in natural hazard risk research, assessment and management
  - catalyses research informed dialogue with public and private partners in natural hazard risk reduction and resilience activities
- Fund and facilitate the application of research into natural hazard management policy and practice:
  - inform far-sighted, effective risk treatment policy and practice by individuals, sector professionals and other decision makers in the natural hazard management community
  - enhance the effectiveness of EQC and its partners in helping New Zealanders to recover from natural disasters
  - collaborate with industry and government partners to ensure strong leverage of research and education investment

How we measure performance

The results from EQC's research programs accrue over a number of years and results are tracked through both the Output Class Statements of Service Performance Measures and longer-term evaluation programmes. Setting an agreed long term evaluation framework with measures for the Sector is a key deliverable in 2017-18. The performance measures show line of sight to EQC's Strategic Outcomes, and the 2015 National Statement of Science Investment[12].

Expected revenue and proposed expenses

Output three has no expected revenue. Proposed expenses for Output three are $21.8 million. These expenses include budgeted expenditure for GeoNet ($12.3 million).

12 http://www.mbie.govt.nz/info-services/science-innovation/pdf-library/NSSI%20Final%20Document%202015.pdf

Performance measures

Table Three: Output Three Performance Measures and Targets 2017-18

OUTPUTS	MEASURES	TARGETS 2017-18
Fund high-quality natural hazard research and information projects	■ Continued support of investigator-led research to encourage emerging talent and new ideas ■ Biennial grants, university grants, post-graduate student awards and capability grants achieve key research objectives ■ High quality research standard is maintained through a peer review process for completed research reports ■ GeoNet achieves all contracted objectives	■ At least 20% of research grants and sponsorships awarded to investigator-led research ■ 90% of current grants on track to meeting key research objectives; 95% of completed grants meet key research objectives ■ 95% of research reports within one year after completion have undergone third-party peer review ■ All objectives met or on track to be met
Disseminate EQC funded and facilitated research and natural hazard information	■ Funded reports are published / presented in sector print media and/or presented at conferences or stakeholder workshops ■ Number of requests and enquiries for access to EQC's publicly available collections[13] ■ The Research Investment Monitoring and Evaluation Framework demonstrates EQC's ability to capture the impact of HRM through medium to long term progress	■ 90% of completed research reports published or presented in 2017-18 ■ 50 per year ■ The Framework targets for six monthly measurement, are agreed in 2017-18 for 2018-19 implementation
Fund and facilitate the application of research into natural hazard management policy and practice	■ Continued use of EQC's expertise or resources in national or regional Hazard Risk Management (HRM) policy, planning or co-ordinating forums etc. ■ Industry and local government partnership projects to improve natural hazard management capacity and capability meet key contracted project objectives ■ Minerva loss modelling tool incorporates robust up to date earthquake science to inform claims and loss forecasting capabilities for New Zealand	■ Evidence that EQC people and resources are engaging in all relevant areas of HRM policy, planning and coordinating activities ■ 90% of current projects on track to meeting key research objectives; 95% of completed projects met key objectives ■ 90% of relevant reinsurer and research stakeholders report they are satisfied with Minerva development or outputs

13 Grant recipients under our programmes for public good research are required to provide a final report and abstracts on completion. These are listed on our website and are publicly available to interested parties on request.

Output Four: Education

A function under the EQC Act is to facilitate research and education about:

- matters relevant to natural disaster damage;
- methods of reducing or preventing natural disaster damage; and
- the insurance provided under the Act.

The prime responsibility for being prepared for natural disasters lies with homeowners. However, they need information and guidance on the most effective and prudent measures to take to mitigate the risk of damage and physical harm, and on what to expect of EQC should they experience natural disaster damage. EQC's legislation does not permit EQC to carry out mitigation activities for home owners, so EQC cannot directly affect levels of disaster mitigation activity. Instead, EQC pursues nationwide and regional initiatives educating the New Zealand public on ways to reduce and prevent natural disaster damage and encouraging them to take action (public education).The Canterbury earthquakes have provided an opportunity to harness the lessons learned for the future and take advantage of increased public interest in natural hazards.

Output objectives

The objectives for this output are to:

- increase public awareness of, and provide education of, earthquake safety and natural hazard mitigation measures; and
- improve home-owners' understanding of EQC's role should they experience natural disaster damage.

The results from EQC's public education programmes accrue over a number of years with the results being tracked through both annual surveys and longer-term evaluation programmes for Output three – Research.

How we measure performance

The targets for this Output Class are measured by external surveys conducted by agents contracted to EQC (Nielsen's).

Expected revenue and proposed expenses

Output four has no expected revenue. Proposed expenses for Output four are $2.9 million.

Performance measures

Table Four: Output Four Performance Measures and Targets 2017-18

OUTPUTS	MEASURES	TARGETS 2017-18
EQC works with partners to extend the reach of its messages relating to how homeowners can prepare their homes against natural hazards	■ EQC works with strategic partners, including all Territorial Authorities, to extend the reach of home preparedness messages ■ EQC works with ICNZ to ensure homeowners better understand the importance of home and content insurance	■ 3.3m New Zealanders are exposed to EQC's messaging ■ EQC supports strategic partners to promote home preparedness[14] ■ New Zealand's penetration rates for house insurance are at 98% or greater[15] ■ New Zealand's penetration rates for contents insurance are at 78% or greater[16]
Educate New Zealanders to take action to prepare for natural hazards	■ The Fix. Fasten. Don't Forget. programme extends to cover home preparedness for all natural hazards, covered by EQC ■ New Zealanders take action to prepare their homes for natural hazards	■ New information[17] live by December 2017 ■ Greater than 40%[18]
Support New Zealanders when a natural hazard event has occurred	■ After an event, homeowners know how EQC can help and what to do to lodge a claim.	■ EQC provides information using mainstream, paid and social media to reach 90% of homeowners in event area ■ Relevant government agencies[19], local authorities and NGOs have EQC event-specific information[19] to share with their stakeholders

14 This includes museum sponsorships to increase knowledge of natural hazards and encourage families to prepare their homes against damage from natural hazards, research that leads to improved home resilience, and other initiatives such as the Wellington City Council's Resilient Homes project.
15 Source: May 2016, UMR Quarterly Survey for ICNZ
16 Source: May 2016, UMR Quarterly Survey for ICNZ
17 Expanded Fix Fasten Don't Forget content
18 Source: Nielsen's Quarterly Survey
19 For example, Ministry of Civil Defence and Emergency Management
20 For example, advertising, fact sheets, community briefings

PART 2: PROSPECTIVE FINANCIAL STATEMENTS 2017-18, 2018-19

2.1 Statement of Comprehensive Revenue and Expense

	BUDGET 2018 $(000)	FORECAST 2019 $(000)
EARNED PREMIUMS		
Gross earned premiums	285,856	288,730
Outward reinsurance premium expense	(164,120)	(150,000)
Net earned premium revenue	**121,736**	**138,730**
UNDERWRITING COSTS		
Reinsurance and other recoveries	1,447	48
Claims reduction/(expense)	89,533	(34,524)
Unexpired risk liability reduction	102,515	1,510
Total underwriting movements	**193,495**	**(32,966)**
Surplus from insurance activities	**315,231**	**105,764**
OTHER OPERATING EXPENSE		
Catastrophe response programme	(32,715)	(29,433)
Public education	(2,902)	(2,938)
Research (excluding GeoNet)	(9,719)	(8,736)
GeoNet programme	(12,033)	(12,154)
Total operating revenue and expense	**(57,369)**	**(53,261)**
INVESTMENT ACTIVITIES		
Investment revenue	0	0
Investment costs	0	0
Interest on cash balances	0	0
Revenue from investment activities	**0**	**0**
Crown underwriting fee	(10,000)	(10,000)
Total comprehensive revenue and expense for the period	**247,862**	**42,503**

2.2 Statement of Changes in Equity

	BUDGET 2018 $(000)	FORECAST 2019 $(000)
NATURAL DISASTER FUND		
Capitalised reverses	1,500,000	1,500,000
RETAINED EARNINGS		
Opening balance at 1 July	(2,363,474)	(2,115,612)
Total comprehensive revenue and expense for the period	247,862	42,503
Closing balance at 30 June	**(2,115,612)**	**(2,073,109)**
Closing balance at 30 June	**(615,612)**	**(573,109)**

2.3 Prospective Statement of Financial Position

	BUDGET 2018 $(000)	FORECAST 2019 $(000)
NATURAL DISASTER FUND		
Capitalised reserves	1,500,000	1,500,000
Retained earnings	(2,115,612)	(2,073,109)
Total Equity	**(615,612)**	**(573,109)**
ASSETS		
Premiums receivable	54,843	55,391
Reinsurance and other recoveries	9,754	0
Other receivables	7,040	0
Prepayments	29,455	29,455
Investments	0	0
Property, plant and equipment	14,991	15,198
Intangible assets	31,761	28,902
Total Assets	**147,844**	**128,946**
LIABILITIES		
Bank	(456,103)	(510,374)
Trade and other payables	(12,345)	(14,254)
Provisions	(9)	(9)
Outstanding claims liability	(143,931)	(27,860)
Unearned premium liability	(151,068)	(149,558)
Total Liabilities	**(763,456)**	**(702,055)**
Net liabilities*	**(615,612)**	**(573,109)**

* The Crown has confirmed, in writing to the Commission, its intention to meet its obligation under Section 16 of the Act, to ensure that the Commission can meet all its liabilities as they fall due.

2.4 Prospective Statement of Cash Flows

	BUDGET 2018 $(000)	FORECAST 2019 $(000)
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash was provided from:		
Interest	0	0
Premiums	285,313	288,181
Reinsurance and other recoveries	176,737	9,803
Net GST	37,500	10,000
Cash was applied to:		
Outward reinsurance	(164,120)	(150,000)
Crown underwriting fee	(10,000)	(10,000)
Claims settlements and handling costs	(1,165,180)	(151,595)
Employees and other operating expenses	(36,248)	(29,202)
GeoNet operating expense	(9,043)	(9,224)
Research grants	(5,873)	(5,736)
Net cash outflow from operating activities	**(890,914)**	**(47,773)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash was provided from:		
Sale of investments	0	0
Interest on investments	0	0
Cash was applied to:		
Purchase of property, plant and equipment	(3,225)	(3,497)
Purchase of intangibles	(10,162)	(3,000)
Net cash inflow from investing activities	**(13,387)**	**(6,497)**
Net increase in cash	**(904,301)**	**(54,270)**
Add opening cash brought forward	448,198	(456,103)
Ending cash carried forward	**(456,103)**	**(510,374)**

2.5 Notes to the Financial Statements

Note 1 Prospective Operating Expenditure Excluding Claims Costs

	BUDGET 2018 $(000)	FORECAST 2019 $(000)
Advertising and publicity	2,334	2,221
Amortisation of intangibles	3,792	5,859
Fees paid to the auditor		
– Audit of the financial statements	75	120
Commissioners' fees	343	343
Consultants and contractors	8,352	3,357
Depreciation	3,212	3,289
Employee remuneration and benefits	12,619	12,550
Grants for earthquake research	4,942	4,798
GeoNet operating costs	9,043	9,224
Office rental	1,095	951
Sponsorships	700	700
Superannuation contribution costs	404	311
Technology costs	7,729	7,522
Other administration costs	2,730	2,015
Total operating costs (excluding claims expense and claims handling expense)	**57,369**	**53,261**
EXPENDITURE GROUPED BY FUNCTION		
Catastrophe response programme	32,715	29,433
Public education	2,902	2,938
Research (excluding GeoNet)	9,719	8,736
GeoNet programme	12,033	12,154
Investment costs	0	0
Total expenditure by function excluding claims costs	**57,369**	**53,261**

Note 2 Claims Expense

	2018 CURRENT YEAR $(000)	2018 PRIOR YEARS $(000)	2018 TOTAL $(000)	2019 CURRENT YEAR $(000)	2019 PRIOR YEARS $(000)	2019 TOTAL $(000)
Gross claims – undiscounted	(50,000)		(50,000)	(50,000)		(50,000)
Movement in discount		(8,337)	(8,337)		(484)	(484)
Amortisation of risk margin		147,870	147,870		15,960	15,960
Gross claims discounted	**(50,000)**	**139,533**	**89,533**	**(50,000)**	**15,475**	**(34,524)**

2.6 Significant Accounting Policies

Reporting Entity

The Earthquake Commission (the Commission) is a Crown Entity as defined by the Crown Entities Act 2004 and is domiciled in and operates in New Zealand. The relevant legislation governing the Commission's operations includes the Crown Entities Act 2004 and the Earthquake Commission Act 1993 (EQC Act). The Commission's ultimate parent is the New Zealand Crown.

The Commission's primary objectives are to administer the insurance against natural disaster damage as provided for under the EQC Act, facilitate research and education about matters relevant to natural disaster damage, and to manage the Natural Disaster Fund (the Fund) including the arrangement of reinsurance.

The Commission has designated itself as a public benefit entity (PBE) for financial reporting purposes.

The reporting period covered by these prospective financial statements is for the years ending 30 June 2018 and 30 June 2019.

Basis of Preparation

Measurement Base

The financial statements have been prepared on an historical cost basis modified by the measurement of financial instruments at fair value through surplus or deficit, and the measurement of insurance liabilities and reinsurance recoveries at present value as set out below.

Functional and Presentational Currency

These financial statements are presented in New Zealand dollars, which is the functional currency of the Commission, and are rounded to the nearest thousand dollars.

Going Concern

Actuarial estimates of the Commission's claims liabilities indicate that total liabilities exceed its assets after accounting for reinsurance. The Crown has confirmed in writing to the Commission its intention to meet its obligation under Section 16 of the EQC Act to ensure that the Commission can meet all its liabilities as they fall due. Section 16 states: "If the assets of the Commission (including the money for the time being in the Fund) are not sufficient to meet the liabilities of the Commission, the Minister shall, without further appropriation than this section, provide to the Commission out of public money such sums by way of grant or advance as may be necessary to meet the deficiency upon such terms and conditions as the Minister determines".

The Board has therefore adopted the going concern assumption in preparing these financial statements.

Statement of Compliance

These prospective financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice. They comply with FRS 42 and other applicable financial reporting standards, as appropriate for public benefit entities. The accounting policies set out below have been applied consistently to all periods presented in these prospective financial statements.

Accounting Judgements and Major Sources of Estimation

The preparation of financial statements in conformity with Tier 1 PBE accounting standards requires judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, revenue and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised (if the revision affects only that period) or in the period of the revision and future periods (if the revision affects both current and future periods).

The actuarial judgements and estimations involved in measuring insurance liabilities and reinsurance recoveries are key areas of estimation where the assumptions made may have a significant effect on the financial statements, with a significant risk of material adjustment in future periods. The magnitude and number of Canterbury earthquakes have resulted in a higher than usual level of uncertainty associated with this measurement.

Insurance

Gross Earned Premiums

Premium income is recognised using the 24ths method to approximate the contract period over which the premiums are earned. The underlying assumption of the 24ths method is that all premiums booked during a particular month can be approximated by an annual policy that incepts during the middle of the month. Premiums not earned at balance date are disclosed in the Statement of Financial Position as an unearned premium liability. Premiums receivable are reported net of discounts paid to collecting agencies.

Outward Reinsurance Premium Expense

Premiums paid to reinsurers are recognised by the Commission as outward reinsurance premium expense in the Statement of Comprehensive Revenue and Expense from the attachment date over the period of indemnity of the reinsurance contract, in accordance with the expected pattern of the incidence of risk. Prepaid reinsurance premiums are included in prepayments in the Statement of Financial Position.

Reinsurance and Other (Reductions)/Recoveries

Reinsurance recoveries are the expected reimbursement of claims settlements and claims handling costs that the Commission can recover under its reinsurance contracts. Other recoveries may include the reimbursement of expenditure incurred on behalf of other parties (predominantly the Crown or Crown entities).

Reinsurance and other (reductions)/recoveries received or receivable on paid claims, reported claims not yet paid, claims incurred but not reported (IBNR), and claims incurred but not enough reported (IBNER) are recognised as revenue in the Statement of Comprehensive Revenue and Expense. They are measured as the present value of the expected future receipts, calculated on the same basis as the liability for outstanding claims.

Claims (Expense)/Reduction

Claims expenditure represents payments for claims, claims handling costs, the movement in the liability for outstanding claims and the associated risk margin.

The outstanding claims liability is recognised at balance date as the central estimate of the present value of the expected future payments for claims incurred to balance date, with an additional risk margin to allow for the inherent uncertainty in the central estimate. The expected future payments include those in relation to claims reported but not yet paid, IBNR, IBNER and claims handling costs.

The outstanding claims liability, comprising all unpaid claims and claims handling expenses related to claims incurred prior to the end of the reporting period, is valued in accordance with the Professional Standard No 4 (General Insurance Business) of the New Zealand Society of Actuaries and PBE IFRS 4 – Insurance Contracts.

The risk margin associated with an event is amortised over the financial year to reflect a reduction in uncertainty within the central estimate as increased numbers of claims are settled.

Unexpired Risk Liability (Increase)/Reduction

At balance date, the Commission assesses the adequacy of the unearned premium liability by applying the liability adequacy test as specified by PBE IFRS 4 – Insurance Contracts. The liability adequacy test determines whether the Commission's unearned premiums at balance date are sufficient to cover future claims arising from existing contracts.

The liability adequacy test compares the current estimate of the present value of the expected future cash flows relating to claims arising from the rights and obligations under current insurance contracts (with an additional risk margin included to allow for the inherent uncertainty), to the value of the unearned premium liability. If the value of the unearned premium liability is exceeded, the movement is recognised in the Statement of Comprehensive Revenue and Expense and recorded in the Statement of Financial Position as an unexpired risk liability.

Assets Backing Insurance Liabilities

All assets of the Commission back its insurance liabilities in accordance with Section 13(3) of the EQC Act, which states: "All money in bank accounts established by the Commission, and all investments and other assets of the Commission, shall be deemed to form part of the Fund".

Grant Payments

The Commission provides discretionary grants for earthquake research and research dissemination. Discretionary grants are those where the Commission has no obligation to award on receipt of the grant application and are recognised as expenditure when the contract is executed to ensure the performance criteria, on which approval of the grant was based, are met.

Foreign Currency

Foreign currency transactions are translated into New Zealand dollars using the exchange rates prevailing at the transaction date. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation, at year-end exchange rates, of monetary assets and liabilities, are recognised in the Statement of Comprehensive Revenue and Expense.

Taxation

The Commission is exempt from the payment of income tax in terms of the Income Tax Act 2007. Accordingly, no charge for income tax has been provided for.

The Commission pays transactional taxes such as Goods and Services Tax, Fringe Benefit Tax and Non-Resident Withholding Tax.

Goods and Services Tax (GST)

All items in the financial statements are presented exclusive of GST, except for receivables and payables, which are presented on a GST inclusive basis. Where GST is not recoverable it is recognised as part of the related asset or expense.

Net GST receivable or payable at balance date is included in receivables or payables in the Statement of Financial Position as appropriate. Commitments and contingencies are disclosed exclusive of GST.

The net GST paid or received, including the GST relating to investing and financing activities, is classified as an operating cash flow in the Statement of Cash Flows.

Investments

Interest

Interest income is accrued using the effective interest method.

Realised Gains and Losses

Income from investments includes realised gains and losses on all investments, including currency gains and losses, and gains and losses on the sale of assets.

Unrealised Gains and Losses

Income from investments includes unrealised gains and losses on all investments, including currency gains and losses.

Financial Instruments

A financial instrument is recognised if the Commission becomes a party to the contractual provisions of the instrument. A financial asset is derecognised if the Commission's contractual rights to the cash flows from the financial asset expire or if the Commission transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Purchases and sales of financial assets are accounted for at the date that the Commission commits itself to purchase or sell the asset. Financial liabilities are derecognised if the Commission's obligations specified in the contract expire or are discharged or cancelled.

Bank

Cash comprises cash balances, cash in transit, bank call deposits and term deposits of less than three months. The carrying amount of cash approximates its fair value.

Investments

All investment assets held by the Commission are to meet insurance liabilities and are therefore designated at fair value through surplus or deficit.

Fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active, fair values for initial recognition and, where appropriate, subsequent measurement is established by using valuation techniques.

Receivables

Receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Receivables with a maturity date within 12 months of the reporting date are recognised in current assets in the notes to the Statement of Financial Position while those with maturities greater than 12 months are recognised as non-current. Receivables are carried at amortised cost using the effective interest method less any impairment.

Other Financial Assets

Other financial assets are initially measured at fair value and subsequently measured at amortised cost using the effective interest method, less any impairment losses.

Trade and Other Payables

Trade and other payables are recognised when the Commission becomes obliged to make future payments resulting from the purchase of goods and services. These are measured at amortised cost.

Property, Plant and Equipment

Overview

Property, plant and equipment is recorded at cost less accumulated depreciation and accumulated impairment losses.

Additions

The cost of an item of property, plant and equipment is recognised as an asset only when it is probable that future economic benefits or service potential associated with the item will flow to the Commission and the cost of the item can be measured reliably. Where an asset is acquired at no cost, or for a nominal cost, it is recognised at fair value when control over the asset is obtained.

Disposals

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount of the asset. Gains and losses are recognised in the Statement of Comprehensive Revenue and Expense, in the period in which the transaction occurs.

Subsequent Costs

Costs incurred subsequent to initial acquisition are capitalised only when it is probable that the future economic benefits or service potential associated with the item will flow to the Commission and the cost of the item can be measured reliably.

The costs of day-to-day servicing of property, plant and equipment are recognised in the Statement of Comprehensive Revenue and Expense in the period in which the transaction occurs.

GeoNet Assets

GNS Science administers the design, engineering, operation and maintenance of New Zealand's geological hazard monitoring system (GeoNet) under an agreement with the Commission. The services performed by GNS Science include the purchase, testing, installation and commissioning of capital equipment on behalf of the Commission.

The GeoNet assets, comprising buildings, computer equipment and other equipment, remain the property of the Commission and are included in the Commission's property, plant and equipment in the Statement of Financial Position.

Realised gains and losses arising from the disposal of property, plant and equipment are recognised in the Statement of Comprehensive Revenue and Expense in the period in which the transaction occurs.

Depreciation

Depreciation is charged on a straight-line basis at rates calculated to allocate the cost or valuation of an item of property, plant and equipment, less any estimated residual value, over its estimated useful life. The estimated useful lives of different classes of property, plant and equipment are reviewed annually and are as follows:

Furniture and equipment	2-10 years
Leasehold improvements	0-12.2 years
Computer hardware	3 years
Canterbury event furniture and equipment	1-11.8 years
Canterbury event motor vehicles	3 years
Canterbury event computer hardware	1.5-2.5 years
GeoNet buildings	25 years
GeoNet computer equipment	3 years
GeoNet other equipment	8 years

Intangible Assets

Intangible assets are recorded at cost less accumulated amortisation and impairment losses.

Research and Development

Expenditure on research activities, undertaken with the prospect of gaining new scientific knowledge or understanding, is recognised in the Statement of Comprehensive Revenue and Expense when incurred. The Commission does not undertake development of new products or processes other than software referred to below.

Software Acquisition and Development

Software development expenditure is capitalised only if development costs can be measured reliably, the product or process is technically and commercially feasible, future economic benefits are probable, and the Commission intends to and has sufficient resources to complete development and to use or sell the asset. The expenditure capitalised includes the cost of materials, direct labour, and overhead costs that are directly attributable to preparing the asset for its intended use. Other development expenditure is recognised in the Statement of Comprehensive Revenue and Expense when incurred.

Capitalised software development expenditure is measured at cost less accumulated amortisation and accumulated impairment losses.

Subsequent Costs

Costs incurred subsequent to initial acquisition are capitalised only when it is probable that the future economic benefits or service potential associated with the item will flow to the Commission and the cost of the item can be measured reliably.

The costs of day-to-day servicing of intangible assets are recognised in the Statement of Comprehensive Revenue and Expense in the period in which the transaction occurs.

Intangible assets are amortised on a straight-line basis at rates calculated to allocate the cost or valuation of an item of intangible assets, less any estimated residual value, over its estimated useful life. The estimated useful lives of different classes of intangible assets are reviewed annually and are as follows:

Computer software	3 years
Canterbury event software	1.5-3 years

Impairment of Non-Financial Assets

The carrying amounts of the Commission's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. For intangible assets that are not yet available for use, the recoverable amount is estimated at each reporting date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised immediately in the Statement of Comprehensive Revenue and Expense.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell. Value in use is depreciated replacement cost for an asset where the future economic benefits or service potential of the asset:

- are not primarily dependent on the asset's ability to generate net cash inflows; or
- the Commission would, if deprived of the asset, replace its remaining future economic benefits or service potential.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Leases

Operating leases, where the lessor substantially retains the risks and rewards of ownership, are recognised in a systematic manner over the term of the lease. Lease incentives received are recognised evenly over the term of the lease as a reduction in lease expense.

Liabilities (Other than Insurance)

The Commission recognises a liability when there is a present obligation (legal or constructive) as the result of a past event, it is probable that expenditure will be required to settle the obligation, and a reliable estimate can be made of the obligation. Where the timing or amount of the obligation is uncertain the obligation is recognised as a provision.

Employee Entitlements

Employee entitlements include salaries and wages, annual leave, long service leave and other similar benefits which are recognised in the Statement of Comprehensive Revenue and Expense when they accrue to employees. Employee entitlements to be settled within 12 months are reported at their undiscounted nominal value. The liability for long service leave is calculated based on the present value of likely future entitlements accruing to employees, based on years of service, years to entitlement, the likelihood that employees will reach entitlement and contractual entitlements information.

Other Liabilities and Provisions

Other liabilities and provisions are recorded at the estimated fair value of the expenditure required to settle the obligation. Liabilities and provisions to be settled beyond 12 months are recorded at their discounted value. The increase in a discounted provision due to the passage of time is recognised as a finance cost.

Contingent Liabilities

A contingent liability is disclosed when a possible obligation arises from past events, whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Commission. A contingent liability is also disclosed when a present obligation arising from past events is not recognised because it is not probable that settlement of the obligation will result in a cost to the Commission, or the amount of the obligation cannot be measured with sufficient reliability.

Superannuation Schemes

Defined Contribution Schemes

Obligations for contributions to the KiwiSaver and the State Sector Retirement Savings Scheme (SSRSS) are accounted for as defined contribution superannuation schemes and are recognised as an expense in the Statement of Comprehensive Revenue and Expense on an accruals basis.

Cost Allocation

Expenditure of the Commission is allocated across its four main functions: catastrophe response programme, public education, research (excluding GeoNet), and investment costs. Expenditure is allocated to these functions by directly attributing costs as far as possible and by the apportioning of indirect costs based on the average number of full time equivalents employed in each function during the financial year.

2.7 Disclosures in relation to prospective financial statements

Major assumptions underlying the prospective financial statements

- In order to meet claims payments over the foreseeable future and continue as a going concern, Section 16 of the EQC Act will be enacted for the Crown to provide guaranteed funding for cash flow requirements.
- Claims costs directly related to the occurrence of major events, and the claims they produce, have not been forecast. $50 million per annum has been provided for other claims settlements and fees.
- Growth in the residential housing stock of 1% per annum.
- No change in Government policy in respect of Crown fees, taxation or premium levy rates.
- Reinsurance costs are based on management estimates prior to the 2017/18 round of negotiations.
- Estimates for events claim expenses, liabilities and cash flows are based on the December 2016 actuarial update prepared by Melville Jessup Weaver.
- The following actuarial assumptions were used in determining the claims liability at that date:

Weighted average term to settlement	0.77 years
Claims inflation rate per annum	2.5%
Demand surge per annum	15%
Discount rate per annum	2.02%-2.91%
Risk margin	17.9%
Claims handling expense ratio	7.0%

Purpose of prospective financial statements

These prospective financial statements have been prepared for internal management purposes and for inclusion in the Statement of Performance Expectation.

Degree of uncertainty attaching to prospective financial statements

a. *Return rates on New Zealand Government securities are based on data provided by the New Zealand Treasury but actual results are subject to market variables.*

b. *No estimate for future major events, or costs directly associated with them, has been made, due to the high level of uncertainty in any estimate.*

c. *Some key sources of actuarial uncertainty in relation to Canterbury estimates include: complexity of remaining claims and the impact of reopened claims in relation to remedial issues and financial reconciliations with insurers and reinsurers.*

Factors that may lead to material differences between prospective financial statements and the actual financial results prepared in future reporting period

a. *The occurrence of further earthquakes or other natural disasters covered by the Commission could significantly impact on future actual financial statements.*

b. *Changes in any of the actuarial assumptions noted above could result in changes to the Commission's claims liability.*

c. *Reinsurance premiums are based on estimates made prior to renewal of contracts for the 2017-18 year and actual premiums paid may differ from estimates due to changes in rates charged by reinsurers and levels of cover achieved.*

Cautionary Note

Actual financial results achieved for the period covered are likely to vary from the information presented, and the variations may be material.

Responsibility and Approval

The prospective financial statements were approved by the Board of the Commission on 27 March 2017. The Board of the Commission is responsible for the prospective financial statements presented, including the appropriateness of the assumptions underlying the prospective financial statements and all other required disclosures.

Actual financial results are not incorporated in the prospective financial statements. The Commission does not intend to update the prospective financial statements subsequent to presentation.

These prospective financial statements comply with NZ IFRS.

OUTPUT CLASS	REVENUE	EXPENDITURE
1. Administration of the EQC Act, insurance scheme and Natural Disaster Fund	$285.9 million	$174.1 million
2. Claims handling and the catastrophe response programme (Customer Services)	Nil	$32.7 million
3. Research	Nil	$21.8 million
4. Public education	Nil	$2.9 million

EARTHQUAKE COMMISSION
Kōmihana Rūwhenua

New Zealand Government