CLAIMS AUDIT

PROVIDING THE CLAIMS REVIEW YOU DESERVE

(03) 365 4460
office@ksl.co.nz

LOCATION:
KSL Audit Limited
18-20 Fitzgerald Avenue
Christchurch 8011

POSTAL:
KSL Audit Limited
PO Box 1344
Christchurch 8140

ksl.co.nz

17 December 2018

Mr Daniel O'Grady
Principal Policy Advisor
Financial Markets
Policy Building Resources and Markets
15 Stout Street
Wellington

Ms Deborah Salter
Senior Policy Advisor
Financial Markets
Policy Building Resources and Markets
15 Stout Street
Wellington

Dear Daniel and Deborah

The following has been prepared as a result of an interview that KSL Audit management had with you both in relation to regulation of the New Zealand Insurance industry.

Directors of KSL Audit are:

Kevin Seque Managing Director and the principal of the KSL Insurance Group of companies has had over 47 years' experience in the life and general Insurance Industry.

Jack Radford Independent Director, formerly Chartered Accountant and Head, Department of Accounting, Economics and Finance at Lincoln University (retired)

Brian P Kreft Chairman of the KSL Group.
Formerly a Principal of Forsyth Barr Limited
Chairman of Les Mills Holdings Ltd & Les Mills International Ltd
Chairman Generation Group Ltd
Formerly chairman of share broking firm Hamilton Hindin Greene Ltd (retired 2018)
Formerly Deputy Chairman of the New Zealand Stock Exchange Market Surveillance Panel.

KSL Audit Limited (KSL) is an insurance advocacy company based in Christchurch that has been involved in the settlement of in excess of 300 earthquake claims. Of the last 184 claims settled and surveyed, KSL has achieved an average increase of $434,162 per claim over the initial offer first presented by the Insurer. Each claim has taken up to two years to negotiate and fortunately none of these claims have had to revert to the court for legal intervention. KSL has a robust, authoritative and pragmatic settlement process based on expert evidence and robust negotiation.

HOW KSL BECAME INVOLVED

Kevin Seque was approached by three clients who were having difficulty getting satisfactory assessment and settlement offers for their claims. From assisting these clients, through word of mouth and client referral, KSL created a separate Earthquake Claims Audit business. This business subsequently settled over 300 claims (and been involved in the negotiation of over 400). As a result of the robustness of the systems and processes, no claim settlements have required legal intervention.

The EQC Class Action Agreement

KSL identified early in 2011 that the inappropriate manner in which EQC were assessing and administering claims, required legal intervention. It was obvious that most home owners did not have the necessary insurance claims knowledge or the understanding of how and what professional reports were required to prove their loss. Further, in the majority of cases they did not have financial capacity to employ advocates and/or lawyers.

Initially as a 'social good' KSL Audit assisted in establishing a core group of EQC claimants and introduced the group to Peter Woods of Anthony Harper Barrister and Solicitors, Christchurch. Anthony Harper who agreed to proceed with a class action on the group's behalf. A copy of the settlement agreement with EQC is included in appendix 1.

Even after the settlement statement was released to the public, EQC continued to usurp their role and responsibilities by failing to observe the agreement and administer the claims in accordance with the Act.

A further disadvantage for homeowners who did not have independent financial means was that, because they were still deemed to be under cap, no payment was made to them by EQC. This meant, in most instances, that they had no financial capacity to secure professional advice or evidence to support their claims. In a lot of instances, they were unable to gain access to further lines of credit from their bank or mortgagee because the earthquake damaged home was their only security.

Where homeowners were overcap and the funds paid to their bank (or them personally) they were able to use such funds, in the first instance, to secure professional advice and evidence to support their proof of loss.

It is important that within any future planning, consideration must be given to homeowners for them to have access to funding to enable them to establish and/or develop their proof of loss evidence and/or engage Advocacy Services. There should be a provision for these costs to be a specified sum insured item forming part of the homeowner's insurance policy. Refer page 14, bullet point 4.

Political Interference

Politically induced Interference in the claim's settlement process commenced early in the Canterbury Earthquake Sequence. (CES)

1. **MBIE Guidelines**

   The Government introduced in December 2010, The Department of Building and Housing Guidelines then known as the "DBH guidelines.
   This document and subsequent amendments was to provide a guide to best practice repairs after an earthquake disaster.

In actual fact this document, on its own, has caused an estimated 85-90% of all of the disputes between Homeowners, Advocates, Lawyers and EQC and the Insurance Industry.
Whilst I am sure "well meaning" initially, the Insurance Industry and EQC for financial advantaged, conveniently "seized upon" this lower threshold of building standard and substituted this document as the accepted standard for repair, overlooking the statement at page 15 of the December 2010 Guidance document. It states: *some insurance policies may require a higher standard of reinstatement than set out in column 2 of table 2.3.*
The Ministry of Business, Innovation & Employment (MBIE) Guidance Document for repairing and rebuilding houses affected by the Canterbury earthquakes has been used by both EQC and the Insurers.
This document does not have any jurisdiction over the policy or claim and it openly states that "repair methodologies recommended may not satisfy the requirements of the insurance policy".
The MBIE guidelines clearly states that it is issued as "guidance" under section 175 of the Building Act 2004, and states "While the Ministry has taken care in preparing this document, it is only a guide and, if used, does not relieve any person of the obligation to consider any matter to which that information relates, according to the circumstances of the particular case." Refer appendix 8 "Clarification of MBIE's Role".

These standards included dislevelment target levels of:
- 25 mm horizontal dislevelment and
- 10mm lateral stretch as the target measurement for determining new foundation reinstatement standards rather than the existing building code standards as specified in the EQ Act and the policy.

These levels were subsequently amended after the Boxing day 2010 earthquake to 50mm horizontal and 20mm lateral and 10mm verticality over 2.4M respectively with the caveat "some insurance policies may require a higher standard of repair than those outlined within this document".

The building code standards at this time in force relevant to the above included:

Construction Standards for timber framed buildings: *NZS 3604 states the maximum deviation from horizontal for a timber framed building is **5 mm in 10 m**, or a total of 10 mm over any length over 10 m. The clearest requirement for floor level tolerances for houses is stated in Table 2 of NZS 3124:1987. The variation in bearing surfaces for timber in NZS 3124 is required to be within **±5 mm** and the maximum depression between two high spots 3 m apart on a floor is to be 8 mm.*

Construction Standards for Wall Verticality Tolerances *Building tolerances for residential buildings are as follows: **5.0mm Plumb** tolerance to wall framing refers to NZS 3604: 2011 Table 2.1.*

Contrary to the DBH caveat and the requirement that all policies and the EQC Act must observe "any cost of compliance with Government or local authority bylaw or regulations" EQC adopted these standards from day 1. Ultimately the use of these guidelines was overturned by the Anthony Harper EQC Action Group in an out of court settlement but EQC continued to use same unless legally challenged.

Unfortunately, whilst the media statement confirmed that the EQ Act was and would always be administered as agreed, the reality was the staff of EQC and their appointed assessors, engineers and building surveyors continued to inspect and assess properties utilising these MBIE levels and standards as their benchmark.

Initially the Insurance industry chose to adopt the policy standard. After the February 22, 2011 earthquake event the MBIE reinstatement guidelines were adopted.

IAG and Southern Response were the first, and the rest of the insurance companies followed shortly thereafter.

Our anecdotal information is that in the early years of the CES there were weekly insurance industry management meetings. Co-incidentally, if a process was implemented by one insurer, then within days, the rest of the Insurers adopted similar strategies.

2. EQC's Standard of Repair Issues

KSL Audit clients obtained in 17th August 2017 the legal opinion from Anthony Harper determining EQC'S standard of repair obligation, Appendix 5.

The Earthquake Commission Act 1993 provides that EQC will cover homeowners for "replacement value" (subject to the $100,000 plus GST cap) which is defined as follows:

"*any cost which would be reasonably incurred in respect of –*

(a) Demolition and removal of debris, to the extent that it is essential to enable the building to be replaced or reinstated; and
(b) Replacing or reinstating the building to a condition substantially the same as, but not better or more extensive than its condition when new, modified as necessary to comply with any
applicable laws; and
(c) Complying with any applicable laws in relation to the replacement or reinstatement of the building; and
(d) Other fees or costs payable in the course of replacing or reinstating the building, including architects' fees, surveyors' fees, and fees payable to local authorities …";

The standard of repair can be summarised as:

(a) equal to, but not necessarily identical to, the original building;
(b) using building materials and methods in common use; and
(c) code compliant.

This requires EQC to pay for repairs which recreate the original functionality, relative quality and aesthetic appearance. It is something which is equal to but not necessarily identical to the original.

EQC is also:

(a) liable for the cost of any additional work that is required to ensure that the work is code compliant;
(b) liable for the cost of working on undamaged parts of the home, if that work is necessary to repair the damaged parts of the home; and

(c) required to repair floor dislevelment (and out of wall verticality), even if historic settlement is also present and will also be rectified.

In situations when EQC elects to pay rather than repair, it must assess the cost of repair based on the standard of repair set out above. It is not entitled to use Clause 9(1)(a), Schedule 3 when assessing the cost as that provides that when EQC elects to repair it "*shall not be bound to replace exactly or completely, but only as circumstances permit and in a reasonably sufficient manner …*".

KSL Audit Footnote.
The original purpose of Schedule 3 clause 9 (1) (a) by the Act's Authors was to capture the 100 year old home built of Kauri or some other type of construction element or method no longer available or in common use or practice.
KSL Audit and its supporting legal advice and, as per the Group Action Agreement, consider that this was never intended to be applied to each and every EQC claim.
Refer Appendix 1,2,5

3. EQ Act Schedule 3 clause 9 *(1) (a)*

Along with the MBIE guidelines after February 22, 2011, EQC adopted the following section of the EQ Act in isolation and we understand this is a breach of Trite law by interpreting an Act of Parliament in isolation of the overall principal meaning of the Act. EQC by settling claims and/or reinstating homes using this exception and lesser standard for assessment and repairs failed to meet the requirement of the Act.

Within the Group Action Agreement* it was confirmed that cash settlements must be assessed to the primary principals of the EQ Act.

"Replacing or reinstating the building to a condition substantially the same as, but not better or more extensive than its condition when new, modified as necessary to comply with any applicable laws";

For managed repairs, Schedule 3 could apply, but in the majority of cases, "circumstances did permit" however the repairs that were undertaken were to a lesser standard than the EQ Act and the policy required.

There were a significant number of EQC claims that did not meet the KSL criteria for contracting KSL, yet still required assistance. KSL Audit assembled a significant group and approached Anthony Harper to assist them. The numbers grew through public meetings to over 150 and became referred to as the "EQC Action Group". The Group won an Agreement against EQC***

KSL Audit had firsthand insight into the EQC management behaviour before and after this "out of court" agreement and settlement. refer appendix 1 attached

KSL Audit can state that there was no change to the day to day operational behaviour of EQC staff with respect to assessing and settling claims. In fact, following the public announcement claims continued to be withheld from being declared overcap, as per the schedule attached, (appendix 7) which supports this statement.

Every one of these claims was ultimately declared overcap and the final settlements are "eye watering". Refer summary page 8, the video and appendix 7.

The Public, Politicians and Canterbury Business Leaders and most importantly, Canterbury Homeowners, have been "duped".

The Media release on the Settlement Agreement confirming EQC was managing their claims properly was incorrect. This is evidenced by assessments of houses needing to be reassessed and /or redone before and after this Agreement was signed.

ILLUSTRATIONS OF OUR CONCERNS: THE KSL AUDIT SPONSORED VIDEO.

Prior to the General Election in 2017, KSL Group commissioned and distributed the video appendix 6 **https://vimeo.com/230934913** and **https://youtu.be/NhcsAq_tijg** to all sitting and aspiring politicians as well as Media, Canterbury business leaders and the Insurance industry.

The following is a summary of the disadvantaged homeowners featured in the video.

- Margaret aged 92 came to KSL as an under cap claim in 15/7/2014 and was settled by IAG as a rebuild for $784,459 in 2016
- Sally in her mid-eighties came to KSL in 16/6/2014 as a $148,000 claim was settled by Tower for $541,989 in August 2017.
- June who is in her mid-seventies came to KSL in 18/11/15 as an under cap claim and was settled by IAG as a rebuild for $531,170 in February 2017.
- Tony and Debbie came to KSL in January 2013 as a $259,000 claim. KSL negotiated with Vero a settlement of $663,206 which KSL advised the client, was not sufficient to reinstate their two year old home. They settled in November 2018 with Vero after seeking legal assistance for $1,145,053.
- Mark and Anita came to KSL on 9th December 2014 with a settlement offer of $313,416. KSL recommended that they seek legal assistance when Southern Response refused to accept their engineering position and offered a settlement of $498,221 KSL considered this to be insufficient based on the clients evidence portfolio. They subsequently have been offered $535,000 and have now commissioned further engineering input and assistance from the new Government Residential Advisory Service.

Despite the Government's commitment to "rectifying the wrongs", it has not made any attempt to contact KSL for commentary or input into the proposed Insurance Contract Law review or the restructuring of EQC processes.

KSL developed the video with the objective of creating a "real life" awareness of the issues Canterbury homeowners have endured for over seven years. It presented solutions on how to avert this administrative blunder for the future, so that no other New Zealanders should have to endure the nightmare or the social and/or economic costs created because of:

- An ill prepared and incompetently managed EQC.
- Opportunistic insurance industry management and staff, being incentivised to minimise claims settlements.
- Inaccurate assessment processes.
- Inappropriate and non-consented repairs.
- Inappropriate substandard MBIE repair guidelines.
- An ineffective dispute resolution process.

KSL can state with certainty that, based on visible and actual experience working within the current processes and performance indicators, the EQC and Insurance industry remain ill-equipped to manage the next major natural disaster.

HOW KSL AUDIT SELECTED THE CLAIMS & CLAIMANTS

Kevin Seque has spent 47 years plus in the insurance industry and has had significant Insurance and claims management experience including a past role as State Insurance Business Manager/accountant and Claims Auditor.

Since 1980 Kevin has been the Managing Director of KSL Insurance Limited, an Insurance and financial planning business. Since 1999 the business has been involved in the residential investment property sector.

In 2001 Kevin Seque developed Aurum Property and Aurum Property Systems Limited (Aurum) was incorporated in 2003. Aurum had facilitated the financing, design, engineering, permitting and construction of in excess of 400 houses for residential property investors in Christchurch, Wanaka Queenstown, Nelson and Wellington. From 2008 to the present this Company has focused on owner occupier clients and from 2011 to 2018 on rebuilding the homes of property owners that KSL Audit has settled claims for. Aurum has constructed in excess of 150 New homes ranging in value from $380,000 to $2,300,000. Aurum changed its name in 2018 to "Aurum Building Brokers Limited" to better reflect its current business model.

Having had the experience of assessing and investigating claims, together with Kevin's background in property construction, he became well versed in identifying earthquake damage to residential properties. KSL Audit has focused on assisting clients with difficult and significant (over $500,000) claims, particularly on TC3 sites, flood management and coastal areas and hillside properties. Clients were generally referred to KSL Audit, where there was a high degree of complexity required in designing foundation solutions and negotiating reinstatement settlements.

Geographic location

KSL had no geographical restriction; our focus was based on clients who had genuine earthquake claims that presented as significant repair/rebuilds.

The construction professionals network that Aurum had established over the previous 10 years, were contracted to provide initial inspection reports and costings and develop the evidence required by homeowners to support their claims that their properties had suffered earthquake damage and the reinstatement solutions required to meet the standard of repair in terms of their policies.

KSL Audit provided to each professional a standard of repair instruction that was agreed between the Insurer, KSL Audit and KSL's Audit legal advisers Anthony Harper. Appendix 4.

KSL Audit developed, for each client, a portfolio of evidence that was used as the basis for negotiating claim settlements with insurers consistent with the Jardin vs Lumley 2014 decision (Justice Kos confirmed that it was "the homeowners obligation to present best evidence").

KSL Audit did not advertise its services, Homeowners came to KSL Audit by referral from other clients when they could no longer rely on the Insurer or EQC's scoping and assessment, resulting in the low offers being presented under "full and final settlement". Our statistics support and justify their concerns and reasoning for appointing KSL Audit. Refer Appendix 6 and 7.

KSL Audit did not take on minor (EQC undercap) claims unless the claim was clearly at first inspection deemed by KSL Audit a "significant and serious" repair (over $300,000). Refer Appendix 6 and 7.

KSL Audit would only take on claims that were genuine Earthquake damaged property claims and where KSL Audit was satisfied the homeowner was not receiving their fair entitlements under their Insurance policy.

Evidence of the impact of KSL Audit's Intervention is amplified in Appendix 6 and 7.

EQC FINANCIAL FAILURE TO INSURED HOMEOWNERS

Evidence outlined below is representative of a much larger impropriety by EQC staff and management.
As KSL Audit has previously stated it did not take on undercap claims. However, of the 68 claims accepted as undercap initially only 3 remain in ongoing EQC debate the other 65 have all been settled as overcap claims.

EQC Analysis for 2017

	Cumulative	Individual settlements
"Undercaps" cumulative EQC assessments	$ 2,425,495	$89,833
KSL Audit cumulative settlement	$14,723,710	$545,322
Total cumulative settlement increase sum	$12,298,214	$455,489

KSL's average under cap claim in 2017 was $545,322

The point KSL Audit is demonstrating is that this is "Mum and Dad New Zealand" being clearly disadvantaged by a Government Agency even after an out of court Settlement Agreement confirmed the Act was being administered incorrectly, yet still being misinterpreted.

Footnote: Media reports indicate there are thousands of "botched and re-repairs" with estimates being projected between $500M and $1 Billion. KSL believes this is still understated.

INSURERS CONTRACTUAL OBLIGATIONS

Based on our experience as evidenced in this document, the exclusion in relating to contracts of insurance provided for in section 46L subsection 4(d) of the Fair Trading Act requires reconsideration

Since June 2011 KSL has settled over 300 claims. Our analysis of our claims since 2014 indicates the significance of the predatory behaviour of the Insurance Industry in taking advantage of the inequality in contractual 'power' between the insurance companies and policy owners.

A summary is as follows:

186 Claims	**Total**	**Ave. per house**
Offers received when KSL Audit appointed	$53,781,946	$289,150
Settlement offers negotiated by KSL Audit	$134,875,218	$725,135
Increase over initial offer	$80,754,271	$434,162
Average increase as a percentage per claim		251%

This summary suggests that without our intervention 186 homeowners could have been exploited by their claims being settled for over $80 million less than what they eventually received. This is surely inconsistent behaviour for a self-regulating industry that promotes an collective behaviour based on "good faith".

THE CASE FOR TIGHTER REGULATORY CONTROLS.

The evidence presented in the preceding section supports the need for the Insurance Industry to have strict regulatory controls, together with revised best practice standards for claims management.

Based on our experience we have observed the following as being contributing factors to the failure of the Insurance Industry to honour "good faith" principles.

Apportionment (*apportioning damage to various claims events).*
The Insurers went to court for a declaratory judgement over "apportionment".

Exacerbation (*a worsening of the damage or an increase in the deformation, making something that is already damaged or broken worse. A new claim should only be lodged if there is clearly defined new damage. Existing damage worsening is not a new claim)*

The Insurers and EQC developed an extensive advertising campaign encouraging EQC claimants to make multiple claims "or they could miss out" without advising what the financial impact on the homeowner would be nor what exacerbation meant. This has caused thousands of claimants to remain needlessly undercap.
This advertising campaign resulted in significant cost to NZ tax payers as a result of EQC having to fund additional claims over and above the statutory $100,000 cap. However, this resulted in a 'windfall' gain for the private insurers who avoided meeting significant claim costs which should have fallen to them. This wealth transfer should be easily quantifiable by EQC.

EQC and Private Insurers Staff Training Failure

EQC and the private insurers must accept the responsibility for failure to train their staff and contractors on how to quantify and determine if further claims were correct and appropriate to lodge.

Tax Payer Cost

The Tax Payer has had to fund not only the EQC reinsurance shortfall, but also the AMI / Southern Response bailout. There is also the unquantifiable social cost on the public health system caused by the above staff training failure compounding incorrect EQC assessment of undercap claimants living in damp, mouldy, cold and broken houses and the tactics of insurers applying multiple inspections, unjustifiably low offers and operating to the '*delay deny and defend*' disaster management strategy.

Staff Bonuses, Early Settlements, and Financial Inducements

Anecdotal information from ex insurance company employees that insurers were paying claims staff bonuses and offering financial inducements and incentives to staff for "under paying" and under settling valid claims. A report tabled in Parliament in 2016 recorded that Southern Response staff received bonuses for understating claims settlements, under the guise of "early settlement bonuses" to a reported amount of $3.1m.

Plain Language Policies:

In our opinion the worst example of the lack of good faith is the Insurance Industry going to the court for direction on how to interpret their '*plain language policies*'**.**

The IAG policy

"We will pay the cost of repairing or rebuilding the home to a condition as similar as possible to when it was new, using current materials and methods, and any cost of compliance with Government or local authority bylaw or regulations." I would have thought is self-explanatory or

The Southern Response AMI policy

"We will pay to repair or rebuild the home to an **"as new**" condition up to the floor area stated in the policy schedule. We will use building materials and construction methods in common use at the time of repair or rebuilding. If your house is damaged beyond economic repair you can choose any one of the following options: To rebuild on the same site we will pay the full replacement value cost of rebuilding your house." Or

The Vero policy

"We will pay – at **our** option
The cost incurred in rebuilding or repairing the damaged portion of the home using currently equivalent building materials and techniques to a standard or specification no more extensive, nor better than its condition **when new"** or

The Tower Policy

"The full replacement value of your house at the situation.
We will use building materials and construction methods commonly used at the time of loss or damage. We are not bound to pay the cost of replacement or repair beyond what is **reasonable, practical or comparable with the original**.
Full replacement value means the cost actually incurred to rebuild replace or repair your house to the same condition and extent as when new and up to the same area as shown in

the certificate of insurance, plus any decks, undeveloped basements, carports and detached domestic buildings, with no limit to the sum insured".

The EQC Standard

"Replacing or reinstating the building to a condition substantially the same as but not better or more extensive than its condition **when new**, modified as necessary to comply with any applicable laws".

MBIE

The hierarchy of an insurance policy claims process management is accepted as:

1. The Policy
2. The Building Act
3. The Building Code
4. Local Authority bylaws
5. The MBIE guidelines

With simple clearly defined plain language good faith contracts, and the known and understood Insurance policy hierarchy as above, it seems incredulous that supposedly ethical institutions like insurance companies would need to seek the guidance of the courts to define and determine what "as new" "as when new" and "when it was new" or "as comparable with original" means.

THE INSURANCE CONTRACT LAW REVIEW

Kevin Seque having been involved actively in developing submissions over his many years of involvement within the Insurance industry made a conscious decision not to provide a formal presentation to MBIE on "the Insurance contract law review', for the following reasons:

> *"We believe that this review once 'sanitised' by the Insurance Industry lobby group, will be another inept, watered down document that will, like the Fair Insurance Code, sound virtuous and meaningful, but will culminate in the poor unsuspecting policy holder and the NZ tax payer being required to contribute yet again to an incompetent government agency (EQC) and the unregulated Insurance elites if further catastrophic events occur."*

It was for these reasons that KSL Audit commissioned the video using "true life" examples and supporting recommendations advocating for a Government Agency to regulate and supervise the New Zealand Insurance Industry and EQC. A set of clearly defined rules for not only the sale and underwriting of a policy but also a similar set of rules for settling claims with a maximum of 24 months for insurers to settle all claims for national disaster events. Normal claims should be required to be settled within 6 months. Both sets of obligations (sales and claims) to be administered by a "fast track" Complaints Authority with wide ranging powers to protect the insuring public of New Zealand**.**

The KSL proposal

To prevent the problem that homeowners have experienced in obtaining fair, efficient, and timely settlement of their claims as a consequence of the Canterbury 2010 and 2011 earthquake events, regulations need to be introduced to:

a) protect the taxpayer from needing to underwrite EQC insolvency or Insurance Company default at claims time for any future catastrophic events.
b) ensure the Insurance Industry doctrine of ", delay, deny and defend" be outlawed by an aggressively supervised regulatory timetable for disaster recovery settlements with severe financial penalties for non-performance and breaches of good faith.

Based on the Kevin's day to day involvement in the claims settlement process at both EQC and Insurer level it is evident that the new wave of politicians do not understand the magnitude of the suffering, nor have the political appetite to fix, with urgency, the plight of the many Canterbury homeowners with 100's of "first time" claims still unresolved at EQC and Insurance Companies. Unless they are Canterbury MP's they will not be able to comprehend the extent and magnitude of the claims and the many thousands of "botched" repairs.

This is evidenced by the same EQC and Insurance management continuing to enjoy generous salaries and bonuses yet failing to provide the necessary systems and processes that will finalise with honesty, skill, accuracy and timeliness, the settlement of the balance of the outstanding claims or make good the legitimate claims of homeowners now experiencing the outcomes of "botched" repairs.

The most concerning central issue is that these people and politicians appear to remain totally oblivious to the reality of the outcome, if a similar event occurred in a main centre like Wellington.

In the video, KSL Audit presented 'bullet point' recommendations to remedy this situation for the future (outlined below).

- Self-regulation has failed. The Insurance Industry's behaviour and profiteering must be examined, reigned in and monitored.
- The Industry requires a regulatory body that not only regulates the sale of policies, but also the claims management process. The Regulator needs to have similar scope and authority to those of the Financial Markets Authority with respect to claims administration and settlement.
- Regulatory monitoring and reporting with respect to disaster reinsurance.
- EQC and Insurers must agree a minimum level of capacity and excess exposure to be appropriately reinsured so that the tax payer is not required to "top up" and bail out inadequate disaster exposure reinsurance shortfalls. Natural disaster treaty guidelines would ensure that an AMI situation never occurs again; particularly as all of the major property and life Insurers are now overseas owned.
- Consideration should be given to implementing similar regulation as is required in the financial planning industry under the Financial Adviser Act 2018. This should set down detailed regulatory structure not only relating to the behaviour of an Advisor and the sales process but also to reinsurance, claims management and settlement behaviours of the insurers.

Underwriting at Claim Time (UACT) should be Banned.

A habit "surreptitiously creeping" into the insurance industry is "underwriting at claim time".

- The Insurer accepts the premium and offers a protection contract in the form of Life, trauma, medical, disability, Income protection, or house, contents or car.
- At Claim time the risk is then actually underwritten.
- At Claim time the Insurer then examines the policy holder's medical records, Property condition etc.
- If the insured has not correctly disclosed the status of the risk and therefore does not meet the ***"fine print"*** criteria required to own the contract, the claim is declined or, in some instances, diminished.

To assist the reader to understand the "underwriting at claim time process further:

Life Insurance underwriting

- Life insurance, Trauma and Total and Permanent Disablement.
  As a standard procedure after being "medically" underwritten and issued a Life, Trauma, Total Disablement or Income Protection Insurance policy, at claim time the Insurance Company, currently, has the ability to go back 5 -10 years into the policy owners medical records to determine whether they would have insured you had all the medical records been disclosed (which the insured person gave the Insurer authority to obtain and review within the application disclosure) at the time of purchasing the contract. However, for cost saving and UACT Insurers elect to not get the information at application purchase.

Income Protection Insurance

- Income protection insurance is now being sold on similar medical underwriting terms but in addition, requires not only medical but financial information.
- Financial underwriting.
  At inception (purchase date) of the Income policy, Insurers are requiring that the insured nominate the sum insured the insured wishes to be protected for.
- At claim time the insured person (who is now incapacitated) is required to prove their income that they have earned to the nominated level of income. No payment is made until proof is provided.
  It is far easier to obtain this information from the insured's employer, IRD, or accountant while the insured is healthy, active and applying for the contract, rather than when the insured is disabled and/or incapacitated and generally unable to produce the details without added stress or assistance at claim time.
  Some policies may consider the income established either, during the currency of the contract, or in the past 12 months, or average over the last 3 years, or best 12 months in the past 3 years.
  KSL Audit advises clients that the only product worth owning for certainty (which is the basis of insurance) is a medically and financially underwritten Agreed Value contract.

Medical insurance

- The insurer provides immediate cover without underwriting and at claim time the Insurer then can go back 3, 5 or 10 years or longer into your medical records when you lodge a claim. If a "pre-existing" condition or consultation is recorded, this can be sufficient to become a voidable contract or for that event.

House Insurance

- The insurers have, for the past 15-20 years or more, offered the "ultimate" whistles and bells (comprehensive/Premier) home and contents contracts. However, for expediency and profitability the Insurers failed to exercise diligence in inspecting or ascertaining what they were insuring. They allowed the homes and contents to be insured by brokers, homeowner walk ups to the sales centre, over the phone, or on the internet. They then proceeded to underwrite these same risks at claim time, as can be seen through the Canterbury earthquake sequence (CES)
- Through the earthquake sequence, home claims were being discounted and declined because there were allegedly:
  Non-consented renovations undertaken
  - No code compliance on the property or part thereof
  - Pre-existing damage
  - Deferred maintenance
  - Home owners were being deemed "leaky homes" five and six years after the 2011 CES. KSL has evidence and argued for homeowners that no maintenance had been undertaken resulting in plaster solutions split causing leaks. Spouting had broken and not been replaced causing leaks etc and because it would have mitigated the loss or would have masked the damage.

  Where repairs had been undertaken "masking" the damage, I have personally be in situations where the homeowners were given the "third degree" or accused by inference of trying to profit from their loss. Most Advocates advised clients to minimise their loss by doing what minimal repairs were required to mitigate further damage, but not to do anything that would prejudice the claim. Because some insurers deliberately delayed the inspection assessment and reporting process, weather damage and further separation naturally occurred that could have been prevented had the insurer been more responsive to reinstatement of the homeowner's property.

  KSL Audit has evidence of claims where insurer timelines exceeded 1 year for the insurer to present a settlement offer to the homeowner. This is after the Insurer receiving EQC overcap evidence, the KSL portfolio of evidence and then conducting their own assessments taking a further 12-18 months to compile their own evidence and present a settlement offer.

- The Insurers assessment and case manager representatives had an attitude of, "if we can't see it, or it has been repaired, it is either pre-existing or not earthquake damage".

  If the property was inspected at application time (as they all previously were in the 1980's and 1990's) prior to the policy being issued, there would be no conversation about the homes condition at claim time. However, as part of the deny, defer, delay and defend mantra it is, now, the insurers word against the homeowners on the condition of the property.

To avoid this claims behaviour in the future, insurance policies should not be allowed to be sold until the property is inspected, or if not inspected at inception the Insurer should not be allowed to decline or diminish a claim later.

Accident Compensation Commission (ACC)

The ACC is a monopolistic business managed along the same lines as EQC and is an out of control bureaucracy. The ACC structure and claims management should be considered as part of this recommended claims review.
A code of practice and claims accountability process are long overdue within this organisation.

Disclosure and Acceptance at Inception.

Regulators need to be cognisant that the Consumer is naive in the ways of Insurance and requires financial certainty and protection from an industry that pays "lip service" to the Fair Insurance Code, encourages confrontation and legal action rather than seeking settlement by way of fair and transparent investigation and if a dispute arises be resolved through reasonable negotiation and finally binding mediation.

- Clearly defined Rules and Regulations should be developed
- The application questionnaire must be clear and concise and easy to understand
- All applications for Insurance be underwritten at purchase.
- Once submitted to the underwriter if further information is required from answers received on the application the following should occur:

Life insurance

- The medical attendant records should be requested and/or
  a medical and /or a blood test should be requested
- A policy condition could be that, if a claim occurs within the first 3 years and a medical condition or lifestyle habit has not been disclosed the policy will be void/voidable
- After 3 years the Insurer should have no ability to decline the claim for any form of medical non disclosure.
- Premium may need to be revised to ensure that more medicals are requested
- Lower underwriting limits may need to be considered by the Insurer.
- More underwriting care will need to be undertaken by Insurers prior to accepting insurance policies so that they are not transferring the risk back onto the naive and insurance illiterate New Zealand insuring public.

Homeowner Insurance

- The insurers offered the "ultimate" (comprehensive/Premier) contracts but failed to exercise diligence in inspecting what they were insuring (caveat emptor) and allowed the homes to be underwritten at claim time for expediency and profit. Regulators should ban such practices.
- An inspection should be undertaken of each risk by a qualified building consultant/surveyor.

- Gradual deterioration should not be allowed to be used as a means of declining policies. Homeowners are generally not aware of leaks in roofs and walls etc i.e. leaky homes.
- Defects should be identified at time of underwriting the risk by the insurance company.
- The Insurer should in every case review the local authority property file prior to acceptance of a risk.

INSURANCE INDUSTRY REGULATIONS

Regulations must be drafted by the regulators incorporating ACC, Life, Health, Fire, General Motor, Liability, Marine and Consumer protection and any other insurance offer to the public. The objective is to restore confidence and integrity in the insurance industry and to offer certainty to the NZ insuring public as they are, largely, naive on the finer points until a claim arises.

Insurance Company Objections

Insurers will argue that:

1. Regulations are not required and will defend their position on good faith and fairness
2. Regulations will increase the product pricing to consumers.
3. Only a small percentage of claims are affected by non-disclosure, exacerbation, deferred maintenance ,gradual leaking etc
4. Only approximately 14% of claims go under the "claims spotlight"
5. The current process works, vis a vis for consumer certainty from regulation and diligent underwriting, it does not warrant the extra cost involved in carrying out individual inspections and medical attendants' reports.

KSL Audit and others concerned and/or affected consumers disagree.

KSL Audit's involvement with claimants over the past 40 years and the Canterbury earthquake claimants over the past 7 years bears testament to the need for regulation. There are clients that 7 years on still having their homes reinspected for the multiple time and being told that their earthquake damaged house is subject to pre-existing damage or deferred maintenance because they could not/did not fix the problem for fear of "masking" the damage to both EQC and the Insurer. Refer to the many stuff /press Media reports on outstanding claims.

POLICY WORDINGS
All Policies Should:

- be written in clear concise plain language terms.
- be written and able to be interpreted in plain language to a 16-year-old persons' understanding.
- offer no ability for the Insurer to seek legal clarification on its own policy terms and conditions and particularly not at claim time under current contracts. if the Insurer is in doubt and wishes to alter the terms and conditions of their contracts, they have the ability to cancel or amend any Fire and General contract with 7 or 14 days' notice, (then the market can decide the quality of their product). Unlike life insurance contracts which

cannot be changed once issued by the Insurer. The current policy and benefits are preserved.

- All insurance policies should offer the ability to include within the policy and pricing a minimum sum insured provision of, say, $40,000 or option to purchase a greater sum for the development of the owners' proof of loss evidence, necessary to prove their claim. (Similar to rewriting of records or claims preparation cover under a loss of profits contract).
  The CES has shown that many homeowners are out of pocket particularly those who repaired or rebuilt their homes as they had to fund their own reports (up to $40,000) as well as pay for the professional fees required to reinstate the property to prove their loss. Undercap EQC claimants who did not receive a cash payment or overcap settlement had in a lot of instances no ability to fund the proof necessary to argue EQC and Insurer assessments. Banks would not release funds where there was a mortgage involved.
- Insurance Companies will be responsible for all aspects of an Earthquake claim. e.g. EQC and policy assessment including EQC overcap payments and full costs incurred settlements.
- an internal process will be established on a "bordereaux" basis for EQC overcap reimbursement by EQC to the Insurer. The Insurer will pay the homeowner or mortgagee immediately the property is determined overcap in the first instance, (an internal Insurer /EQC and Bank agreement will be established and published on the process, to enable the homeowner to access funds to develop their portfolio of evidence to justify proof of claim or to manage temporary repairs.
- provide within the Insurance policy, a very clear and definitive letter of instruction that the engineering assessing community of approved EQC accredited personnel will be required to respond to. This instruction will set out, in plain language, the standard of repair that is required to be met to fulfil the policy obligations. This standard will be understood and used by all professionals to resolve claims correctly, efficiently and competently. On-going industry training on these standards should be mandatory for claims management, loss adjusters, engineers, building surveyors, geotechnical engineers, cadastral surveyors Quantity Surveyors etc. NZQA in association with the Insurance Industry should develop monitor and manage the assessment, training and accreditation and continuing education process.
- KSL Audit estimates this would resolve more than 85% of claims.

Insurance Company Minimum Standards for Claims Management

Insurance staff involved in claims management need to be qualified and trained to fulfil their duties correctly and must possess a thorough understanding of the:

- respective insurance policy requirements
- Insurer's obligation to act in good faith
- Fair Insurance Code.
- Fair Trading Act
- Consumer Guarantees Act

For employees tasked with managing the reinstatement of houses, they must possess a sound understanding and knowledge of the building code, local authority requirements, as well as the Insurers obligations under the:

- Insurance policy requirements
- Earthquake Act,
- Building Act
- To act in good faith

- Fair Insurance code.
- Fair Trading Act
- Consumer Guarantees Act

Future Disaster

- In the event of a major disaster a strategy should already be in place agreed by the Politicians the Civil Defence and other first responder agencies, the Insurance Industry and EQC.
- Within the claims process the Insurer will have the lead role and be responsible for managing the Insurance disaster claims process.
- As soon as the first responder has identified overcap status the cap payment will immediately be paid to the home owner to instigate repairs/develop portfolios of evidence.

Settlement Process in Disaster Situations

- Cash settlement of claims should not be the primary option in the town/city/community the settlement of claims should be undertaken on a cost incurred basis:
- EQC overcap payment on initial determination
- Indemnity payment once claim quantified
- cost incurred payments made as works agreed and undertaken.
- The replacement / total loss settlement to be in accordance with policy terms.
- The objective is to protect the integrity of the current and future housing stock within the town or city and the community by having property repaired correctly.
- It will also protect affected financial markets including the banks and other mortgage interests.

EQC

- EQC be completely overhauled and treated as a first line reinsurer only.
- EQC should never participate in individual claims management.
- The Insurer must take “first responder” position on all claims.
- “Apportionment” and “Exacerbation” must be properly explained to all claims staff as these issues have resulted in duplication of claims and incorrect assessments by EQC.

INSURANCE INDUSTRY DISASTER MANAGEMENT CLAIMS RESTRUCTURE

KSL Audit recommend the development of a panel of qualified professionals within a new restructured regulatory framework for disaster recovery and claims management response.
EQC to acknowledge it is a reinsurance business and the Insurance Industry acknowledge it is the sole claims manager of all future disaster response claims incorporating EQC liability.

- The EQC and Insurance Industry be required to invest in a training program managed and administered by MBIE and NZQA
- The development of a training program that will certify professionals from within the construction, engineering and Loss Adjusting professions.
- A panel of approved assessment professionals is established.
- Only members registered and qualified will be accredited with an Authorisation standard.
- Only Authorised members registered and current on the panel can be used by the Insurance industry to assess and loss adjust claims.

- These professionals must undergo ongoing training and continuous education to remain on the register and be current members of an approved and enforceable professional body which has a code of conduct.
- There must be a fast track disciplinary authority established to oversee compliance with the process.
- In the event of a national disaster the first responders must be assembled and flown and transported into the disaster zones immediately. Triage teams should be set up consisting of an LBP builder and a qualified structural engineer.
- A triage assessment should be undertaken of the area, Street by Street of the damaged property.
- These Professionals should be capable of carrying out an initial assessment to determine minor (undercap) major (overcap) and "marginal" claims.
- Claims can then be reported back to localised headquarters and prioritised into:
    - Damage with security issues
    - Damage with no security issues (cosmetic only)
    - Dampness issues General
    - Elderly home owners
    - Young families with unsafe or damp homes.

  This priority allocation will then be strictly administered

Non-negotiable milestones

- In a National disaster there should be a 2-year maximum deadline on finalising the settlement of all claims or delinquent Insurers suffer significant financial penalties.
- The policy must be clear and concise.
- There must be agreement by the Insurers on the interpretation of policy obligations that homeowners can rely on.
- The Insurance policy document should contain a clearly defined standard of repair that will be issued to the Loss adjuster and all contracted professionals that are involved with claim assessments.
- The EQC / Insurance industry will provide a standard letter of engagement outlining the instructions, scope and format that is required for the preparation of independent “proof of loss” reports.
- All areas of unresolved ambiguity will be addressed by a Government sponsored body convened for that particular purpose and fast tracked.
- A maximum of two duplicate professional reports can be obtained by Insurers to validate damage and quantify loss to compare against homeowners’ proof of loss.

The Insurance Industry objection:

There will, no doubt be significant “pushback” from the Insurance industry on the premise that the proposed requirements will involve extra cost.

The reality is:

- The Insurers appointing only current and qualified assessors from an agreed accredited industry panel will remove duplicate assessments and duplication of claims management and costs.
- Standardising and continual ongoing training and understanding of the accepted policy repair methodology will remove the potential for misunderstandings and identify, clearly, the Insurers obligations.
- After 47 years Insurance sales experience I have first-hand knowledge that the issue of premium is easily countered by the consumer. All they seek is insurance with certainty from credible companies. If it costs a little more to ensure certainty, then they will readily pay the

higher premium for the certainty that the Insurer and EQC have the capacity to pay and the Insurer has the desirability and willingness to pay.

ADDITIONAL ISSUES

First Responder

- A comprehensive first responders program needs to be developed which would see the application and selection of qualified personnel around New Zealand.
- A first responders triage team induction would provide a sound ongoing understanding of the obligations of the EQ Act and the Insurance policies "standard of repair."
- The triage teams would include CPeng registered structural engineers, CPeng registered Geotechnical engineers, Registered building surveyors, Licensed Building Practitioners (construction), Licensed Building Practitioners (Roofing) Certified Loss adjusters, Drainage experts, Foundation specialists, Cadastral Surveyors, Quantity Surveyors, and Specialist Claims Managers.

Land Information Memorandum (LIM)

- Within the reinstatement process it should be mandatory that the local issuing authority insist that all Insurance claim repairs be notified and entered on the LIM to protect future purchasers.
- Insurance settlements on the basis of uneconomic repairs must be recorded on the LIM incorporating the amount paid, scope of works and works undertaken.
- Total Loss assessments should require the demolition and site clearance to be undertaken by the Insurer on settlement of the claim.

Disputes Resolution Process

- There is a need to establish an effective disputes resolution process that is appropriately resourced to deal with major single adverse events such as the Christchurch earthquake.
- The existing Ombudsmen's Office is neither sufficiently resourced nor appropriate to deal with the specific technical and legal issues that have been confronted in this event.
- A specialist tribunal needs to be established to oversee disaster claims with appropriately qualified construction focused experts forming part of the disputes mediation team.
- Fairway Mediation Service was used by IAG and KSL Audit claimants for a short period and it was suspected that because it was a successful IAG ceased funding it.
- This is a model worth reviewing and reconsidering as it was very effective for not only disaster claims but life Health ACC and Fire, General Motor, Marine Liability and Consumer Guarantee Insurance policy issues.

Limitations Act

- Insurers should not have the ability to rely on the Limitations Act as a defence for not meeting their claims obligations.
- A 2-year time limit on all claims will remove this issue in the future.

KEVIN'S SUMMARY OBSERVATIONS

In my insurance career I never considered that I would bear witness to, effectively, the abuse of privilege I have experienced in the past 7 years from within a distorted, conflicted and belligerent Insurance industry.

I have for 47 years represented the Insurance Industry with pride sold product to people under the premise of good faith, certainty and a principled position.

I have shared my understanding of Insurance with many New Zealanders in articles I have written, seminars I have conducted, conferences I have spoken at, lectures I have given in schools and universities promoting the value of owning insurance:

> *"Insurance is about protecting assets that individuals and companies can't afford to lose. Insurance policies (are meant to) offer contracts of certainty, in the form of a document which guarantees an agreed payment if an insured event occurs".*
>
> *Insurance is a a promise to pay, (subject to certain conditions disclosed and agreed at the application date being met).*

Regrettably over the past 7 years through the behaviour I have witnessed and experienced by the EQC Staff, The Staff and Management of the Insurance Industry, The Insurance Council and Individual Insurer company Boards, these principles and the policy promises have not been honoured for policy owners within the Canterbury earthquake insurance community. The spreadsheet Appendix 6 and 7 validate this statement.

Urgency is required by Government to:

- Reign in the "out of control" profit focused insurance companies.
- Restructure EQC and Southern Response to minimize the wasteful cost to the taxpayers who continues to absorb the expense of meetings, restructures, duplicate /multiple engineers and other professionals' costs and legal fees incurred due to the deliberate and cynical behaviour of parties purporting to be acting as claims settlement specialists. These people have abandoned the principals of good faith and proper policy interpretation in favour of hardball tactics resulting in under costed settlements whilst profiteering personally through earning bonuses, promotions and other remuneration benefits.

There is still much to do in Christchurch, to ready New Zealand properly, effectively and efficiently now, to ensure that the problems of Christchurch never again occur.

The changes suggested need political intervention and a willingness and resolve by politicians to "do the right thing" for ordinary New Zealanders.

Please feel free to contact the writer if you require further information to support this Information Memorandum.

Kevin Seque
Managing Director
KSL Audit Limited

Attachments:

1. EQC Group Action Agreement
2. Media Release
3. EQC Assessment confirmed by EQC as instruction to engineers
4. Industry letter of instruction to engineers – IAG and Southern Response
5. EQC legal opinion on Standard of Repair
6. Statistical data of settlements
7. Statistical data of EQC settlements
8. Article on Clarification of MBIE's Role