



Cabinet

CAB Min (11) 27/12

Copy No:

Minute of Decision

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Crown Offer to Residential Insured Property Owners in the Canterbury Earthquake Affected Red Zones: Paper 1

Portfolio: Canterbury Earthquake Recovery

On 18 July 2011, Cabinet:

Background

- 1 **noted** that on 27 June 2011, Cabinet noted a range of decisions taken by a group of Ministers authorised to have Power to Act to take decisions on matters relating to Canterbury earthquake land damage and remediation issues, including:
- 1.1 that insured residential property owners in the Red Zones will have the choice of two offered packages, either:
 - 1.1.1 **Option A:** The Crown will offer to purchase the entire property at the 2007 Capital Value rating valuation (less any land and dwelling insurance payments already made). The Crown will also take an assignment of all earthquake related insurance claims. There will be a process through which any property owners who consider that there is a material discrepancy between the 2007 rating valuation and the market value of their property (e.g. because of subsequent improvements) can raise their concerns; or
 - 1.1.2 **Option B:** The Crown will offer to purchase the land only at the greater of the following (less any EQC land payments already made):
 - 1.1.2.1 2007 Land Value rating valuation; or
 - 1.1.2.2 EQC valuation for the minimum lot size applicable;
 - 1.1.3 that the Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have;

[CAB Min (11) 24/15]

Modification of package

- 2 **noted** that there is some confusion about whether Option B (as outlined in paragraph 1.1.2 above) relates to both the land and the dwelling (i.e. the whole property) or the 'land only';
- 3 **agreed** that the Option B package be reworded as follows:
- 3.1 the Crown will offer to purchase the property at the greater of the following (less any EQC land payments already made):
 - 3.1.1 2007 Land Value rating valuation; or
 - 3.1.2 EQC's actual land settlement under the Earthquake Commission Act 1993;
 - 3.2 the Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have;
- 4 **noted** that in this minute and in subsequent papers Option A and Option B will be referred to as Option 1 and Option 2 respectively;

Purchase option issues relating to unit title ownership

Unit titles – principal insurance policy held by body corporate

- 5 **noted** that under a unit title scheme, the principal insurance policy is usually held by the body corporate and that, unless 75 percent of owners agree otherwise, proceeds of the principal policy must be applied to reinstatement;
- 6 **noted** that under Option 1, if the Crown does not control at least 75 percent of the units and the votes, it will not be able to ensure that a special resolution in relation to the application of the proceeds of the principal insurance policy;
- 7 **noted** that even where the Crown has 75 percent of the units and votes, it could still be subject to 'hold up' risk where owner(s) choose to stay in their unit(s), which would prevent the Crown demolishing the units it owns;
- 8 **noted** that allowing individual unit owners to accept Option 1 of the Crown's offer will enable them to move on with their lives and provide them some future certainty;
- 9 **noted** that Option 2 of the Crown's offer is not possible for unit titles unless all owners agree, as post-sale individual owners do not retain an interest in the principal insurance policy as they are no longer a member of the body corporate;
- 10 **noted** that under a unit title situation with a principal insurance policy held by the body corporate:
- 10.1 it is not possible for some owners to accept Option 1 and others to accept Option 2;
 - 10.2 for Option 2 to be given practical effect, 100 percent of unit owners must agree to accept Option 2, with the body corporate's dwelling claims under the principal insurance policy being assigned to all of the owners jointly;
- 11 **agreed** to allow individual unit owners to accept Option 1 of the Crown offer, but to only allow Option 2 if all owners agree;

- 12 **noted** that the decision in paragraph 11 above allows unit owners to accept at least one of the Crown's offers without the need to obtain their neighbours' consent;

Unit titles – individual insurance policies

- 13 **noted** that in some cases, unit title owners may have their own insurance policies, rather than a principal policy held by the body corporate;
- 14 **agreed** that in the cases referred to in paragraph 13 above, Options 1 and 2 be available to unit title holders, without requiring agreement from the other remaining owners;

Issues relating to cross leases ownership

- 15 **noted** that under a cross lease arrangement:
- 15.1 the owners jointly own the land as tenants in common;
 - 15.2 each individual owner is granted a lease of a specified proportion of the land;
- 16 **noted** that, subject to anything to the contrary in the leases, the Crown will not be able to effectively deal with the land unless it has acquired 100 percent of the interests of the owners;
- 17 **noted** that cross lease properties can either have common walls or can be separate from one another;
- 18 **noted** that under some cross lease arrangements, owners have a joint insurance policy, and that in these cases, unless all the owners assign their interests to the Crown, the Crown will not be able to progress an insurance claim;
- 19 **noted** that under some cross lease arrangements, owners have individual insurance claims, and that 'split acceptances' of the Crown's offer could be workable under this situation;
- 20 **noted** that:
- 20.1 it will be more desirable for the Crown to have 100 percent acceptance of the owners of either Option 1 or Option 2;
 - 20.2 this will stop minority owners trying to delay or derail the process, and it will enable the Crown to progress land or the building claims;
- 21 **noted** that:
- 21.1 the Crown could consider different rules for different insurance situations with cross lease ownership arrangements;
 - 21.2 while this would be more complex and costly to the Crown to complete the purchase transaction, it will provide maximum flexibility to cross lease owners;

- 22 **agreed** to have different rules for different types of cross leased properties:
- 22.1 individual cross lease owners may accept Option 1;
- 22.2 if the cross leased properties have joint insurance, they may only accept Option 2 if they all agree;
- 22.3 if the cross leased properties have individual insurance, each may individually accept Option 2;

Adjustments to purchase price due to incorrect 2007 rating valuation

- 23 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**
- 24 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**
- 25 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**
- 26 **noted** that the Crown has made a offer that is based on pre-earthquake values and at a time when values were at the height of the property boom;
- 27 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**
- 28 **noted** that the purchase price is generous in that it is a value established pre-earthquake and by all accounts in a stronger property market, and that the true market value of the property post-earthquake is dramatically less than the purchase price offered by the Crown;
- 29 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**
- 30 **agreed** that it is not necessary to have any alternative valuation mechanism;
- 31 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**
- 32 **agreed** that, if after an Option 2 offer is signed (including after settlement) the EQC's actual land settlement under the Earthquake Commission Act 1993 is for a higher value than the Land Value, the government agrees to pay a "top-up";
- 33 **authorised** the Chief Executive of the Canterbury Earthquake Recovery Authority to have the discretion, in the instance referred to in paragraph 32 above, to determine the final purchase price and an appropriate date for the top-up option to conclude;

Property owners requesting purchase price adjustments

- 34 **noted** that, to provide certainty and simplicity, the Crown adopted the 2007 Rating Valuations as the purchase price for insured residential properties within the Red Zones;
- 35 **noted** that the 2007 Capital Values of the rating valuations are on average 5 percent higher than recent sales evidence (exclusive of chattels) in the Red Zones, and that this was considered to be a generous pre-earthquake offer to affected residents in the Red Zones;
- 36 **noted** that there are instances where property owners might wish to seek adjustments to the purchase price, for example where:
- 36.1 there is an error of fact on the rating roll (i.e. incorrect dwelling area);

36.2 the owner has undertaken new improvements to the property since the 2007 Rating Valuation was released;

36.3 a property owner subsequently purchased a property at a higher level than the properties 2007 Rating Valuation;

37 **noted** that the Crown's offer to purchase is on the premise that the majority of property owners' equity will be maintained, not actual equity;

38 **noted** that it would raise equity issues and would be unfair to property owners who did not sell, if the Crown adjusted a purchase price to reflect the fact that a property owner purchased property after August 2007 at a higher than its rating valuation;

39 **noted** that the purchase price is generous in that it is a value established pre-earthquake and by all accounts in a stronger property market, and that the true market value of the property post-earthquake is dramatically less than the purchase price offered by the Crown;

40 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**

41 **noted** that a review process could be introduced where property owners provide evidence that they have undertaken improvement work to their property since the 2007 Rating Valuation, and that the value of improvements add 5 percent or more to the property's current rating valuation;

42 **noted** that a request to review would cost the property owner \$500, but that this would be reimbursed if the values changed;

43 **noted** that if the property owner wishes to dispute the revised value, they have 10 days to lodge a written claim with supporting documentary evidence, and that this is assessed by a panel of expert valuers who would make the final determination;

44 **agreed**, in relation to making purchase price adjustments for property owners, that the current Rating Valuation be the purchase price with no amendments, with the exception of factual errors or outstanding building consents that were not taken into account in the 2007 Rating Valuation, which would be amended as per the Valuer-Generals Rules;

The Crown seeking purchase price adjustments for under-insured properties

45 **noted** that a property is under-insured if it is insured for a fixed sum or indemnity value which is less than the purchase price or insured for less than its actual floor area;

46 **noted** that adjusting for under-insurance means that the Crown is not incentivising inadequate insurance cover;

- 47 **agreed**, in relation to making adjustments to the purchase price for under-insured properties, where a property is under-insured by more than 20 percent, to reduce the purchase price on a pro rata basis relative to the percentage that the property is underinsured;

Withheld under sections 9(2)(f)(iv) and 9(2)(g)(i) of the Official Information Act

- 48 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**

- 49 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**

- 50 **Withheld under sections 9 (2)(f)(iv) and 9(2)(g)(i) of the Official Information Act 1982**

The Crown seeking purchase price adjustments – for property owners who have already received insurance/EQC payments for reinstatement

- 51 **noted** that, in some instances, EQC and/or private insurance payments have been made to residential property owners and work has not been undertaken, while other property owners in the Red Zone have spent this money on repair work;

- 52 **noted** that property owners that have not spent payments on repair work are gaining a financial advantage over those who spent the money on repair work, causing an inequity issue;

- 53 **noted** that this will result in a high level of administrative low value deductions, but that the Crown will recoup payments made where the work has not been undertaken;

- 54 **agreed**, in relation to the method by which the Crown can make purchase price adjustments, to only deduct from the purchase price reinstatement payouts and emergency repairs that are more than 5 percent of the purchase price, unless where the property owner has evidence that those payments have been spent on remediation works on that property;

Chattels

- 55 **note** that chattels are defined as blinds, curtains and/or drapes, unfixed carpets, soft-wired (i.e. plug in) and freestanding stoves that are not hardwired, and lightshades;

- 56 **note** that to include these chattels in the Crown's purchase price would be simple and provide certainty to the offer;

- 57 **agreed** that the purchase price be exclusive of chattels, and that the property owner can remove the chattels before settlement (subject to any private insurer salvage rights);

Salvage rights

58 **agreed** that:

- 58.1 in respect of Option 1, the property owner shall deal directly with the Crown's demolition contractor;
- 58.2 in respect of Option 2, the property owner will need to deal directly with the insurer before settlement;

GST

59 **agreed** that the purchase price for the Red Zone properties be rating valuation inclusive of GST, as property owners will either not be required to charge GST or the supply will be zero-rated for GST purposes;

Financial implications

60 **noted** that the financial implications relating to the paper under CAB (11) 429 are outlined in the companion paper under CAB (11) 430 [CAB Min (11) 27/13];

Next steps

- 61 **invited** the Minister for Canterbury Earthquake Recovery to report back to Cabinet in due course on any subsequent decisions that will be required on the treatment of commercial properties and uninsured properties (including vacant lots) in the Red Zones;
- 62 **authorised** the Minister of Finance and the Minister for Canterbury Earthquake Recovery to have Power to Act to take decisions on any minor and technical issues that arise in relation to the above decisions.

Secretary of the Cabinet

Reference: CAB (11) 429; CAB Min (11) 27/13

Office of the Minister for Canterbury Earthquake Recovery

Memorandum for Cabinet

**CROWN OFFER TO RESIDENTIAL INSURED PROPERTY OWNERS IN THE
CANTERBURY EARTHQUAKE AFFECTED RED ZONES – PAPER 1**

Purpose

- 1 This paper seeks the first in a series of policy decisions about the transaction design and implementation for insured residential property owners in the Canterbury Red Zones. It outlines policy issues relating to the purchase price. These transaction design issues are necessary to enable the Crown to make an offer to insured residential property owners in the Red Zones within eight weeks from the announcements of the zone, on 23 June 2011. This paper also highlights financial implications for some of these policy decisions.
- 2 A second paper will follow that covers further transaction design and process and includes policy decisions relating to settlement dates, continued occupation, fast-tracking special cases, deposits, vendor obligations, speculator policy, void policies and bank deed poll. A third paper will cover policy decisions required on non residential insured property such as commercial/industrial land, uninsured land, Crown land, land owned by incorporated societies etc. Additional papers will deal with any announcements of further Red Zones, and any outstanding matters related to the offer process.

Executive Summary

- 3 Ministers with power to act agreed on 22 June 2011 (which was noted by Cabinet on 27 June 2011) to identify four zones of land damage for the greater Christchurch area. This paper relates to the Red Zones, the worse affected residential zones, where rebuilding is not likely to occur in the short-to-medium term. In that decision, Ministers also agreed to extend the choice of two offer packages to insured residential property owners in the Red Zones. Ministers agreed that these options are:

Option A: The Crown will offer to purchase the entire property at the 2007 Capital Value rating valuation (less any land and dwelling insurance payments already made). The Crown will also take an assignment of all earthquake related insurance claims. There will be a process through which any property owners who consider that there is a material discrepancy between the 2007 rating valuation and the market value of their property (e.g. because of subsequent improvements) can raise their concerns.

OR

Option B: The Crown will offer to purchase the land only at the greater of the following (less any EQC land payments already made):

- a) 2007 Land Value rating valuation; or
- b) EQC valuation for the minimum lot size applicable.

The Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have [CAB Min (11) 24/15 refers].

- 4 This is the first Cabinet paper in a series. It seeks decisions regarding:
- clarifying the nature of Option B as there is some confusion about whether it applies to only land or both land and property;
 - purchase option issues relating to unit title ownership;
 - purchase option issues relating to cross lease ownership;
 - adjustments to purchase price due to incorrect 2007 rating valuations;
 - property owners and the Crown seeking purchase price adjustments;
 - insurance excess payments on Settlement;
 - chattels;
 - salvage Rights;
 - GST implications relating to the transaction.

Background

- 5 The 4 September 2010 and 22 February 2011 earthquakes and their aftershocks represent an incomparable natural disaster in New Zealand's history. The aftershocks on Monday 13 June including another M6.3, only served to emphasise the repeated nature of the events and the fact that an endpoint cannot be predicted. The damage in greater Christchurch is unprecedented, in an area of significant population.

- 6 On 22 June, Ministers with power to act agreed to four zones of land damage for Christchurch, based on the severity and extent of land damage, the cost-effectiveness and social impacts of land remediation [CAB Min (11) 24/15]. They are as follows:

Green: There are no significant land damage issues which prevent rebuilding in these areas in the short-to-medium term and rebuilding can begin subject to some conditions.

Orange: Further work is required to determine if rebuilding is likely to be possible in the short-to-medium term. There are 9,770 properties in the Orange Zone with a total rating capital valuation of \$3.762b¹.

White: Following the 13 June 2011 earthquakes which caused further extensive damage these areas require mapping and further assessments to be undertaken.

Red: Rebuilding is not likely to occur in the short-to-medium term due to the obstacles posed by the significant land and infrastructure damage and the high risk of further damage to land and buildings from low-levels of shaking (e.g. aftershocks), flooding or spring tides. There are 5,176 properties in the Red Zone with a total rating capital valuation of \$1.732b.

¹ Figures also include non-residential properties.

Overview of issue

- 7 This paper relates to residential properties identified in the Red Zones announced on 23 June 2011, situated to the east and north-east of Christchurch city and includes parts of Bexléy, Horseshoe Lake, Avonside, Dallington, Burwood East, Richmond, Wainoni & Avondale, Deville Place, New Brighton, Kairaki Beach and Lower Brooklands.
- 8 In designing the processes, we are seeking to give effect to the government recovery objectives where the government is committed to supporting a speedy recovery for people and businesses in the greater Christchurch area, and it accepts the recovery will be a long-term activity and that it is important that recovery is underway quickly. It was with this in mind that the Canterbury Earthquake Recovery (CER) Act 2011 was enacted to ensure that through the Canterbury Earthquake Recovery Authority (CERA) it could among other things:
 - Provide appropriate measures to ensure that greater Christchurch and the councils and their communities respond to, and recover from, the impacts of the Canterbury earthquakes.
 - Enable a focused, timely and expedited recovery.
 - Facilitate, co-ordinate and direct the planning, rebuilding and recovery of affected communities, including the repair and rebuilding of land, infrastructure and other property.
- 9 The price and the process also takes into the consideration the rebuild objectives which were established to assist the Crown in determining where rebuilding can occur or is unlikely to be possible to occur in the short-to-medium term:
 - a) **Certainty** of outcome for home-owner as soon as practicable;
 - b) Create **confidence** for people to be able to move forward with their lives;
 - c) Creating **confidence** in decision making processes (for home-owners, business-owners, insurers and investors);
 - d) Using **the best available information** to inform decisions;
 - e) Having a **simple process** in order to provide clarity and support for land-owners, residents, and businesses in those areas.
- 10 For the purposes of this paper all references to property owners refers to insured residential property owners in the Red Zones, as these are the property-owners to whom the current announcements apply.
- 11 It should be noted that the process for the offer will also be used for any further Red Zones that might be announced, although the timeframes may be adjusted. Whether or not offers should also be available to other categories of property owner will be considered in a subsequent paper.
- 12 Ministers with power to act agreed to extend the choice of two offer packages to insured residential property owners in the Red Zones:

Option A: The Crown will offer to purchase the entire property at the 2007 Capital Value rating valuation (less any land and dwelling insurance payments already

made). The Crown will also take an assignment of all earthquake related insurance claims. There will be a process through which any property owners who consider that there is a material discrepancy between the 2007 rating valuation and the market value of their property (e.g. because of subsequent improvements) can raise their concerns.

OR

Option B: The Crown will offer to purchase the land only at the greater of the following (less any EQC land payments already made):

- a) 2007 Land Value rating valuation; or
- b) EQC valuation for the minimum lot size applicable.

The Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have.

Clarifying the nature of Option B

- 13 In the decisions made by Ministers with power to act on 22 June 2011, and noted by Cabinet on 27 June 2011, Option B was described as:

Option B: The Crown will offer to purchase the land only at the greater of the following (less any EQC land payments already made):

- a) 2007 Land Value rating valuation; or
- b) EQC valuation for the minimum lot size applicable.

The Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have. [CAB Min (11) 24/15 refers].

- 14 The words 'land only' may create confusion as in legal terms both the land and the dwelling will be sold to the Crown (i.e. the whole property). However, property owners will have the opportunity (in conjunction with their insurers) to salvage items from the dwelling, or to relocate or demolish the dwelling. It is preferable under this option that the Crown receives bare land at the time of purchase. To overcome any confusion it is proposed to change the phrase 'land only' in Option B to 'the property'. I also propose that the two options now be referred to as Options 1 and 2 in this and subsequent papers, as this is how they have been referred to publicly.

- 15 I recommend that Option B now be described as:

Option 2: The Crown will offer to purchase the property at the greater of the following (less any EQC land payments already made):

- a) 2007 Land Value rating valuation; or
- b) EQC valuation for the minimum lot size applicable.

The Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have.

Implications under each option for interested parties to the transaction

- 16 Table 1 below outline the rights and obligations of interested parties under Option 1 prior to the Crown agreeing to purchase the property and outlines how the transaction will affect each party post settlement. Table 2 provides the same information for Option 2.

Table 1: Option 1, the sale of a property and assignment of all land and dwelling insurance claims

Option 1	
Land and dwelling plus insurance claims transferred to Crown	
A Key starting rights and obligations pre agreement for sale and purchase	
Insurer	Has rights of salvage over all insured <i>damaged parts, or all of written-off dwelling</i> , until transfer of property (Settlement). If house is a write-off, depending on policy terms, may have demolition obligation. In any event, insurer may opt to demolish dwellings to reduce their potential public liability risk. If house not a write-off, usually obliged to pay repair cost only (including cost of damage debris clearance). Will be expected to pay cash sum for repairs to Crown as assignee.
Bank/Mortgagee	Has mortgage over land and dwelling together. Has contractual rights under mortgages over insurance proceeds. Insured mortgagors need bank/mortgagee permission to sell.
Owner	Has rights of salvage over undamaged parts BUT loses those rights to Crown at time of signing the Agreement. Responsible for all rates, insurance and utility costs up until Settlement
Land and dwelling plus insurance claims transferred to Crown	
B Summary of outcomes of accepting Option 1	
Crown pays	Capital value (Rating Valuation) to owner (net of claims already paid to the property owner).
Crown gets	Land, on Settlement. Dwelling, as is, including fixtures, on Settlement. EQC land insurance claim. EQC dwelling insurance claim. Private insurer dwelling insurance claim.
Owner keeps	Contents, and contents policies. Any outstanding loan debt in respect of property. Chattels (subject to insurer rights of salvage). ²
Bank/Mortgagee	If the Bank consents to the sale, it will release the land security and insurance policy interest.
Insurer	Pays unpaid dwelling claim proceeds to Crown. Has salvage rights over damaged parts of, or written-off, dwellings.
EQC	Pays unpaid dwelling claim proceeds to Crown. Pays unpaid land claim proceeds to Crown.

² Chattels are defined as blinds, curtains and/or drapes, unfixed carpets, soft-wired (i.e. plug in) and freestanding stoves.

Table 2: Option 2 (Sale of property and assignment of EQC land claim only)

Option 2	
Sale of property and assignment of EQC land insurance claim only	
A: Key starting rights and obligations pre agreement for sale and purchase	
Insurer	Has rights of salvage over insured <i>damaged parts, or all of written-off dwelling</i> , until transfer of property (Settlement). If house is a write-off, depending on policy terms, insurers may have demolition obligation. In any event, insurers may opt to demolish dwellings to reduce their potential public liability risk
Bank/Mortgagee	Has mortgage over land and dwelling together. Has contractual rights under mortgages over insurance proceeds. Insured mortgagors need bank/mortgagee permission to sell.
Owner	Salvage rights are between insured and insurer under policy until Settlement.
Sale of property and assignment of EQC land insurance claim only	
B: Summary of outcomes of accepting Option 2	
Crown pays	Land value only (Rating Valuation) to owner (net of EQC land claims already paid to the property owner).
Crown gets	Land, on Settlement. Any remaining dwelling, as is, including fixtures on Settlement. ³ (However, will probably have been salvaged and then demolished by insurer prior to Settlement.) EQC land insurance claim.
Owner keeps	EQC dwelling insurance claim. Insurer dwelling insurance claim. Contents, and contents policies. Any outstanding loan debt in respect of property. Chattels (subject to insurer rights of salvage). ³
Bank/Mortgagee	If the Bank/Mortgagee consents to the sale, it will release the land security but keep a charge over insurance policy proceeds.
Insurer	Pays dwelling claim proceeds to property owner or reinstates home elsewhere, depending on policy terms. Has salvage rights over damaged parts of, or written-off, dwellings.
EQC	Pays unpaid dwelling insurance claim proceeds to property owner. Pays unpaid land insurance claim proceeds to Crown.

- 17 A number of design decisions are required in relation to purchase price polices are required in order that the Crown can make an offer to current owners of insured residential property in the Red Zones.
- 18 In designing the process, we are seeking to give effect to the government objectives of certainty, confidence for property owners and a simple process.

³ Chattels are defined as blinds, curtains and/or drapes, unfixed carpets, soft-wired (i.e. plug in) and freestanding stoves.

Purchase Option issues relating to Unit Titles

19 The options available to property owners with unit titles depend on the type of insurance arrangements in place. I propose that:

19.1 For unit title owners where the principal insurance policy is held by the body corporate, individual unit owners can accept Option 1 of the Crown offer, but can only accept Option 2 if all owners agree

19.2 For unit title owners with individual insurance policies (i.e. there is not a principal insurance policy held by the body corporate), individual owners can choose to accept Option 1 or Option 2, without requiring the agreement of other unit title owners in the body corporate.

20 These two situations are discussed below.

Unit titles – principal insurance policy held by body corporate

- 21 In unit title schemes, the principal insurance policy is normally held by the body corporate. By purchasing a unit, the Crown becomes beneficially entitled to a share of the proceeds of the body corporate's claim under the principal insurance policy. Unless 75% of owners by number and votes agree otherwise, proceeds of the principal insurance policy must be applied to reinstatement. A 75% majority is also generally required to deal with the common property.
- 22 For Option 1, there is no need to assign any claims under the principal insurance policy as part of the sale and purchase process, although the benefit of any insurance held by individual owners would need to be assigned. However, if the Crown does not control at least 75% of the units and the votes, it will not be able to ensure that a special resolution is passed in relation to the application of the proceeds of the principal insurance policy. It may also be subject to "hold-up" risk from other owners, even where it controls 75% of the units and the votes, meaning that some owners may choose to stay on in their unit so the Crown could not demolish the units it owns. This suggests that a minimum acceptance level may be desirable for Option 1.
- 23 Option 2 of the Crown's offer is difficult for unit title developments where the body corporate holds the principal insurance policy. Although it is possible that individual owners will have additional dwelling insurance, it will not be possible for an owner to retain an interest in the principal policy post-sale, because he/she will no longer be a member of the body corporate. The principal policy cannot easily or effectively be split amongst owners. It is however possible for the body corporate's dwelling claims under the principal insurance policy to be assigned to all of the owners jointly, although this in effect would require 100% owner approval.
- 24 In order that the Crown secure 100% ownership and secure the insurance proceeds the Crown would need to negotiate Option 1 purchases with the remaining owners. Until those purchases were negotiated, the Crown would not necessarily be in a position to control the progress of either the land or the dwelling claims.
- 25 In addition, it will not be possible for some unit owners to accept Option 1 (effectively transferring their share in the principal policy to the Crown) while others accept Option 2 (and seek to advance their own dwelling claims under the principal policy for reinstatement on another site).
- 26 For Option 2 to be given practical effect, 100% of unit owners must agree to accept Option 2, with the body corporate's dwelling claims under the principal insurance policy

being assigned to all of the owners jointly. This allows unit owners to accept at least one of the Crown's offers without the need to obtain their neighbours' consent.

Unit titles – individual insurance policies

- 27 In some cases, unit title owners may have their own insurance policies, rather than the body corporate as discussed above. In this case, there is no reason why both Option 1 and 2 should not be available to unit title holders without requiring agreement from the other remaining owners in this case.

Purchase Option issues relating to Cross Leased Properties

- 28 Under a cross lease arrangement, the owners jointly own the land as tenants in common. Each individual owner is then granted a lease of a specified portion of the land. Any un-leased portion of the land is available for common use. Unlike a unit title scheme, there is no body corporate.
- 29 As a result, subject to anything to the contrary in the leases, the Crown will not be able effectively to deal with the land unless it has acquired the interests of 100% of the owners. This suggests that requiring 100% acceptance by cross lease owners may be desirable.
- 30 Dwellings on cross leased properties can have common walls or can be separate from one another.
- 31 In many cases, owners will each have separate dwelling insurance. However, in some cases an insurance policy may be held jointly (e.g. where the dwellings have structural elements in common). In these cases, it may be difficult for the Crown to progress a claim unless all owners have assigned their interests to the Crown. For example, as for unit titles the Crown would not wish to expose itself to some owners accepting Option 1 and some accepting Option 2, leaving the Crown in the position of having to negotiate with other owners in order to progress the dwelling claim. While "split acceptances" could be workable where insurance is not jointly held, it would be simpler, and consistent with the approach outlined for unit titles, to require that Option 2 is only available if all owners agree to accept it.
- 32 The Crown has three options relating to Cross Lease arrangements:
- Cross lease Option A: Have the same rules for all cross leased properties and allow individual cross lease owners to accept Option 1, but only allow Option 2 with an acceptance threshold of 100% of owners.
- Cross lease Option B: Have the same rules for all cross leased properties and offer cross lease owners both Options 1 and 2 with an acceptance threshold of 100% of owners (i.e. 100% must accept Option 1, or 100% must accept Option 2).
- Cross lease Option C: Have different rules for different types of cross leased properties:
- Individual cross lease owners may accept Option 1.
 - If the cross leased properties have joint insurance, they may only accept Option 2 if they all agree.

- If the cross leased properties have individual insurance, each may individually accept Option 2.
- 33 Under Cross lease Option A, in order that the Crown secure 100% ownership and secure the insurance proceeds the Crown would need to negotiate Option 1 purchases with the remaining owners. Until those purchases were negotiated, the Crown would not necessarily be in a position to control the progress of either the land or the dwelling claims.
- 34 Under Cross lease Option B, either all owners must accept Option 1 or all must accept Option 2. A unanimous agreement of owners will stop minority owners trying to delay or derail the process. The Crown would have a greater degree of control over matters once settlement had occurred.
- 35 Under Cross lease Option C, different rules would apply to different insurance situations. Having separate rules will make the Crown's offer more complex to explain to property owners and more complex and costly for the Crown to complete the purchase transactions.
- 36 I recommend Cross lease Option C, as it provides maximum flexibility to cross lease owners.

Adjustments to purchase price due to incorrect 2007 land valuation

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Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

- 38 On 22 June 2011 Ministers with power to act agreed to offer property owners two offer packages. In Option 1 of the offer package it stated that 'there will be a process through which any property owners who consider there is a material discrepancy between the 2007 rating valuation and the market value of their property (e.g. because of subsequent improvements) can raise their concerns.
- 39 As there is confidence in the Capital Values (and as a property's Capital Value is assessed independently of its Land Value, any increase in Land Value would not result in an increase in Capital Value), for those selecting Option 1 no change is considered necessary.
- 40 For those selecting Options 2, they may already choose from the greater of the rateable value of the land or the EQC valuation for the minimum lot size applicable. Although there could be a review process, it will create uncertainty. Since there is already an alternative value available - which has been recently assessed - I consider it is not necessary to have any alternative valuation mechanism.

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

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is therefore proposed that if after an Option 2 offer is signed (including after settlement) the EQC valuation for the minimum lot size is for a higher value than the Land Value, that the government agrees to pay a "top-up". The

Chief Executive of CERA could be given the discretion in this instance to determine the final purchase price and an appropriate date for this option to conclude.

Property owners requesting Purchase Price Adjustments

- 42 Rating valuations are undertaken by territorial authorities who contract out to valuation service providers. Those providers determine rating valuations on behalf of the territorial authority for rating purposes. Under the Rating Valuations Act 1998, the Valuer-General sets minimum standards for rating valuations and maintenance of the district valuation roll which territorial authorities must adhere to.
- 43 In 2007 the Rating Valuations for Christchurch were established and property owners had a right of objection at that time. Following the Canterbury Earthquakes, Ministers with power to act agreed to use the 2007 Rating Valuations as the basis of the Crown offer to insured residential property owners in the Red Zones [CAB Min (11) 24/15 refers].
- 44 The Crown used 2007 rating valuation as the benchmark at which to set the purchase price it was prepared to pay for an individual residential property. This value is well-known and has been open for an appeal process; therefore it meets the objectives of simplicity and certainty.
- 45 The Crown purchase price offer is generally considered to be higher than the property's current market value as it stands currently post earthquake. Analysis (by 'Good Earth Matters' the Christchurch City Council's rating valuers) shows sales exclusive of chattels, for the 12 months ended 3 September 2010, that the average sale price was 95% of the 2007 rating valuation and that 71% (145 sales) sold at or below their rating valuation. While 29% (57 sales) sold above their rating valuation by an average of 7%.
- 46 However there are several instances where residential property owners might wish to seek adjustments to their purchase price. It is expected that these circumstances could include:
- a) Where the 2007 Rating Valuation contains an error i.e. the rating valuation has been assessed on incorrect data such as inaccurate floor area. The Valuer General's rules around errors would remedy this issue by allowing a reassessment of value, along with an objection right.
 - b) Where any new improvement work has been done (including building consents), but the added value of the work is not yet reflected in the 2007 rating value (i.e. for new dwellings or dwelling alterations) the rating valuations rules state that the territorial authority must update the district valuation roll and assess the improvements to the land based on 2007 comparable roll value evidence. Updating the district valuation roll in this manner is called roll maintenance and it also provides for an objection right when a new value is issued.
 - c) Where the property owner has purchased the property after 2007 and at a higher level than its 2007 rating valuation.

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

47 Four options are available to the Crown:

- Valuation Option A: The current Rating Valuation is the purchase price with no amendments with the exception of factual errors or outstanding building consents which would be amended as per the Valuer-Generals Rules; and/or
- Valuation Option B: The current purchase price be amended for any new improvements made to the property since 2007; and/or
- Valuation Option C: The current purchase price be amended where property owners have purchased their property since 2007 and at a higher level than the 2007 rating valuation; and/or
- Valuation Option D: To develop 'a review process' to revise purchase prices where they meet defined criteria as stipulated in paragraph 52.

- 48 As noted above, it is generally considered that the 2007 Rating Valuations Capital Values are on average higher than recent sales evidence in the Red Zones. Based on this analysis, making limited alterations to the rating valuations i.e. Option A would be the most cost effective, timely and straightforward process to implement with most property owners preserving the majority of their equity.
- 49 Option B would acknowledge all improvements to a property since 2007 this would include refurbishments, minor improvement works as well as building work that require building consents. This Option could result in a high number of property owners seeking purchase price reviews for minor alterations to the purchase price. The effect of this option is that it will increase transaction costs to both the Crown and property owner, as well as extending the time taken to confirm a final purchase price.
- 50 Options C and D introduce uncertainty as to a property owners purchase price, and potential inequity as well as adding complexity to the offer process. An example is that these options raise issues of consistency of values across the Red Zones, and issues of fairness and equity for property owners who did not sell in relation to those who purchased a property at a higher level than its rating valuation (eg you could have two identical houses with a rating valuation of \$200,000 but one sold for say \$250,000; so one owner would recoup an extra \$50,000 than another property owner raising issues of fairness and equity), or who did not appeal. This conflicts with the Government's recovery process objectives of a simple offer process and certainty as to outcome for home-owners; although it does potentially increase the confidence of some individual property owners in the decision making process [CAB Min (11) 24/15 refers].
- 51 For Options C and D it should also be noted that it would be difficult to determine the extent to which rating valuations and therefore purchase prices, may increase in the event that values are reviewed. These options would also increase the gross cost to the Crown whilst adding another layer of complexity to the process. It would also confuse what is otherwise a generous and simple offer from the Crown.

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a) Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

b) Withheld under section 9(2)(f)(iv)

c)

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a process could involve lodging a 'request to review' with CERA. The property owner would incur an administration charge to lodge a 'request to review' at a cost of \$500 per property.

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Withheld under section 9(2)(g)(i)

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Withheld under section 9(2)(h)

56 Valuation Option A is preferred.

The Crown seeking Purchase Price Adjustments

57 There are circumstances where it is not appropriate for the Crown to pay the full 2007 Rating Valuation to property owners. This relates to where property owners are under-insured, EQC or private insurance payments have already been spent on reinstating the property.

Each are discussed below.

Withheld under section 9(2)(f)(iv)

Under-Insured Properties

Withheld under section 9(2)(g)(i)

58 Properties are effectively under-insured if the improved property (above ground property) is insured for a fixed sum or indemnity value which is less than the purchase price, or insured for less than its actual floor area. Under-insured properties are covered by EQC cover, as the insurance on the improvements triggers full EQC cover no matter the value of the insurance for the improvements.

59 To address this issue, there are three options available to the Crown:

Under-insured Option A: reduce the purchase price on a pro-rata basis relative to the percentage that the improved property is underinsured; or

Under-insured Option B: where a property is underinsured by more than 20%, reduce the purchase price on a pro-rata basis relative to the percentage that the property is underinsured; or

Under-insured Option C: pay the property owner whose property is underinsured the full rating valuation.

- 60 Under-insured Option C is not preferred, as this would actually involve subsidising the insurance cover purchased, and would be perceived as removing the incentive on property owners to adequately insure themselves and may also be seen as disincentivising the insurance market to offer adequate insurance cover.
- 61 Under-insured Options A and B both allow for adjustments for underinsurance, the difference being that under Option A there would be adjustments for all minor differences. Under Option B there would be a threshold for the adjustments. Option B is preferred as it would be inefficient for the Crown to seek adjust the purchase price for every minor error.
- 62 The threshold level proposed is where the property is underinsured by 20% or more. The threshold is a pragmatic level, based on not wanting to have too high a level (which would perpetuate under-insurance in the future) but considering that a lower threshold (eg 10% variation between the insured value and the value of the improvements) could result in significant transaction costs to administer.
- 63 Option B with a threshold of 20% is my preferred solution to this issue.

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Withheld under section 9(2)(f)(iv)

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Withheld under section 9(2)(g)(i)

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Property Owners already have received insurance/EQC payments for reinstatement

- 69 Some property owners may have already received payments from EQC and/or private insurers for repairs to their homes and work has been undertaken. In this case, the property owner has not received any additional value from these payments as they went directly to making repairs.

- 70 However, there are situations where EQC and/or private insurance payments have been made and work has not been undertaken. In this situation, a property owner in the Red Zones will financially gain from the EQC/private insurer payout plus the full rating valuation for their property. Because other property owners in the Red Zones who paid to undertake the work only receives the rating valuation, effectively causing an inequity issue.
- 71 There are three options available:
- Prior payout Option A: deduct from the purchase price any EQC and/or insurance payments already made, including for repairs except where the property owner has evidence that EQC and/or insurance payments have been spent on remediation works.
- Prior payout Option B: only deduct from the purchase price reinstatement payouts and repairs beyond \$10,000 of the purchase price, except where the property owner has evidence that EQC and/or insurer payments have been spent on remediation works.
- Prior payout Option C: make no adjustments to purchase price for unspent EQC/private insurance payouts made to property owners
- 72 Option A will result in a high level of administration for low value payouts. But the Crown will recoup payments made where the works have not taken place.
- 73 Option B will reduce the administrative work around the Crown recouping a high volume of low value claims, however it will have negative fiscal impacts on the Crown as it will not recoup the full extent of these unspent payments.
- 74 Option C simplifies this issue with no adjustments being made to the purchase price for unspent payouts but the Crown forgoes these claims. The extent of the fiscal implications are uncertain at this time, work is being progressed at present on this issue.
- 75 I consider Option B is the most effective means of ensuring that where significant EQC and/or private insurance payments have been made to property owners and remediation works can not be validated. This option will enable the Crown to recoup major EQC/ private insurance payments made to property owners that have not been spent on repair work.
- 76 Payouts of \$10,000 or more is the threshold proposed before deductions to the purchase price is made where the property owner has already received an EQC and/or private insurance payout and has not undertaken the reinstatement work. The threshold is a pragmatic level, based on not wanting to have too high a level (which would result in some property owners receiving an equity advantage or another property owner who undertook the work) but considering that a lower threshold could result in significant transaction costs to administer.
- 77 Prior Payout Option B is preferred.

Insurance excess payments on Settlement

- 78 Excesses are included in insurance policies to remove the insured party's ability to seek small claims and to ensure that they face some cost of any claim. EQC's dwelling cover has an excess of the greater of \$200 and 1% (i.e. a maximum of \$1,150) per claim.

Some private insurers' dwelling policies have no excess for earthquake claims and others provide for the policy's normal excess.

- 79 Where an excess applies, it applies to each claim so will apply for each different earthquake damage event.
- 80 Excesses are generally deducted at the time of payout. This means that property owners who have received their insurance payout will have paid their excess while those who have unresolved claims will not.
- 81 EQC's land cover has an excess of 10% of the claim with a minimum of \$500 and a maximum of \$5,000. As EQC has not yet paid out any land claims, the Crown will bear this cost.
- 82 In relation to insurance excess payments the Crown has two options available:
- Excess payout Option A: Adjust the purchase price on settlement so that the property owner bears the dwelling excesses.
- Excess payout Option B: Adjust the purchase price on settlement so that the Crown bears the dwelling excesses.
- Excess payout Option C: Adjust the purchase price on settlement so that the Crown bears the EQC dwelling excess but the property owner bears the private insurance excess.
- 83 Option A preserves insurance rights more accurately so property owners bear the dwelling excesses that they agreed to when purchasing their dwelling insurance (or which were imposed by the EQC Act).
- 84 Option B allows property owners to receive the purchase price less any actual cash received, so their total payment (including any EQC or insurance payouts) will be equal to the purchase price.
- 85 Option C is a compromise: the Crown bears the EQC dwelling excess but property owners bear the consequences of choosing an insurance policy that contains an excess for earthquake claims.
- 86 Option C is the preferred option.

Chattels

- 87 The Crown has used the rating valuation as the basis to establish a purchase price. It was the most consistent and fair approach given the number of properties situated in the Red Zones. The purchase price reflects the price the Crown is prepared to pay for the property but a decision is required to establish whether or not the offer price is inclusive of chattels and fixtures.
- 88 For the purposes of this offer chattels are defined as blinds, curtains and/or drapes, unfixed carpets, soft-wired (i.e. plug in) and freestanding stoves that are not hard-wired.
- 89 The Crown has two options available:
- Chattels Option A: That the purchase price is inclusive of chattels.

Chattels Option B: That the purchase price is exclusive of chattels and the property owner can remove them before settlement (subject to any private insurer salvage rights).

- 90 A property is normally sold with chattels included. If the Crown adopts this approach there is certainty for the owner, the insurer, the banks and the Crown as purchaser in what is being sold/purchased. It also creates certainty for salvage as chattels will not be accidentally removed when they should have stayed for the purpose of salvage by the insurer.
- 91 I consider that property owners should be allowed to take their chattels as defined above, subject to any private insurer salvage rights. Discussions with the Insurance Council indicate that the salvage value of chattels varies between insurance companies, and some assess the salvage value of chattels to be zero. Option B will also be favourably received by property owners in the Red Zones.
- 92 Chattels Option B is preferred.

Salvage Rights

- 93 In normal circumstances, the insurer has salvage rights over insured damaged parts, or all of the written off dwelling.
- 94 Under Option 2, the insurer's interest in salvaging the parts of the dwelling in respect of which it has accepted a claim will end on settlement so will need to be exercised before that date. If the property owner wishes to salvage some parts of the dwelling, he or she will need to deal directly with the insurer before settlement.
- 95 Under Option 1, the property owner will transfer both the property and their insurance claim to the Crown, so the Crown will take over the obligation to allow the insurer to salvage those parts of the dwelling in respect of which it has accepted a claim. However, some property owners may wish to salvage undamaged parts of the dwelling (including relocating to another site) and/or their insurer may forgo any salvage rights. There are two options to allow property owners salvage opportunities:
- Option 1 Salvage Option A: Give the property owner a first right of refusal on all salvage by the Crown's demolition contractor.
- Option 1 Salvage Option B: Invite the property owner to deal directly with the Crown's demolition contractor.
- 96 Option 1 Salvage Option B is preferred as it is simpler and less costly to administer.
- 97 Separately, the Crown may agree with some or all of the insurers to contract for demolition on an area-wide basis. If that occurs, insurers would contribute to demolition costs, net of salvage revenue that is available.

GST implications relating to the transaction

- 98 While the Government has announced that it would purchase insured, Red-Zone residential properties at the rating valuation, no decision has yet been made as to whether this purchase price is inclusive or exclusive of Goods and Services Tax (GST).
- 99 In the majority of cases, GST will not be an issue as the property owner will not be GST registered. However, for some property owners, GST may apply to the sale of the property. This will apply when the property owner is GST registered and makes the

sale in the course or furtherance of their taxable activity (which could happen for example, when they used the house as business premises).

- 100 Recent changes to tax legislation now mean that the sale of land between GST registered persons is now subject to GST at 0%, where certain criteria are met. One of the requirements is that the purchaser acquires the land with the intention of using it to make taxable supplies. The requirement is met through Section 5(6) and section 6(1)(b) of the Goods and Services Tax Act 1985.
- 101 If CERA acquires the land from a registered person, the land is deemed to be acquired for the purposes of making taxable supplies and is therefore zero rated.
- 102 As property owners will either not be required to charge GST or the supply will be zero-rated for GST purposes, I propose that the purchase price for the Red-Zone properties be rating valuation inclusive of GST.
- 103 If the property was purchased by the current owner prior to the new tax rules on 1 April 2011 and an input tax credit has been claimed, the owner may gain from the zero-rating on tax by not being required to pay tax on sale. However, this is no different to other transactions between GST registered entities, for which no transitional arrangements apply in relation to the new rules. Furthermore, other examples exist for which GST input tax credits are claimed on purchase but are zero-rated on sale, such as exported goods.

Upcoming Cabinet Decisions

- 104 The following matters will need to be addressed in subsequent Cabinet decisions;
 - a) The treatment of commercial properties in the Red Zones;
 - b) The mechanics of a process to support people in settling their insurance claims, and rebuilding elsewhere;
 - c) The detailed transaction design,
 - Withheld under section 9(2)(g)(i)
 - Withheld under section 9(2)(f)(iv)
 - d) The treatment of Retirement villages in the Red Zones;
 - e) The land management process post settlement;
 - f) The treatment of under insured and not insured in the Red Zones;
 - g) Analysis is also being undertaken on likely new housing – when it will be available, its pricing, together with any barriers to bringing forward any further housing developments.

Announcements

105 I propose the following communications for property owners receiving the offer of purchase:

18 July	<ul style="list-style-type: none"> • Send personalised letter to all Red-Zone property owners outlining the package offer to purchase their land • Building Expo (with property developers, building firms, banking representatives to enable people to consider their future options and commence planning
30-31 July	

Mid-August	<ul style="list-style-type: none"> Recovery Hubs (with insurers, EQC, sub-dividers, geotechnical experts etc) operating in the Red Zone areas
Ongoing	<ul style="list-style-type: none"> Continued conversations with each of the Red-Zone communities to ensure that lines of communication remain effective, people understand the decisions being made and are able to take responsibility and plan for their future.

Next steps

- 106 Subsequent advice will be prepared for Cabinet for decisions on:
- 106.1 Mechanics for implementing decisions on the Red Zones;
 - 106.2 Details of the packages;
 - 106.3 Further support available for home-owners;
 - 106.4 Issues for business owners;
 - 106.5 Issues for the uninsured; and
 - 106.6 Orange Zones

Consultation

- 107 Treasury, Department of Building and Housing, Land Information New Zealand, Crown Law and Ministry of Economic Development were consulted on a draft of this paper.
- 108 Department of the Prime Minister and Cabinet were informed of this paper.

Financial implications

- 109 At this stage, it is difficult to make a firm judgement as to whether the aggregate impact of the decisions in this paper will be to increase or decrease the total costs of acquisition. Any changes, however, are likely to be small relative to the total costs of acquisition. Officials will form more robust estimates of costs over time as better information emerges. As the obligation to purchase red zone properties was incurred in 2010/11, the gross costs of acquisition will need to be validated in the Appropriations (2010/11 Financial Review) Bill.

Human rights implications

- 110 The proposals in this paper are not inconsistent with the New Zealand Bill of Rights Act 1990, or the Human Rights Act 1993.

Legislative implications

- 111 There are no legislative implications arising from this paper.

Regulatory impact and compliance cost statement

- 112 A regulatory impact statement is not required at this time as there are no regulatory changes.

Gender implications

113 There are no gender implications associated with the proposals in this paper.

Disability perspective

114 There are no disability implications associated with the proposals in this paper.

Publicity

115 This is outlined in Paragraph 105 above.

Recommendations

116 It is recommended that Cabinet:

Background

1. **note** on 27 June 2011, Cabinet noted a range of decisions taken by a group of Ministers authorised to take decisions on matters relating to Canterbury earthquake land damage and remediation issues [CAB Min (11) 24/15] including:

1.1 that insured residential property owners in the Red Zones will have the choice of two offered packages either:

1.1.1 **Option A:** The Crown will offer to purchase the entire property at the 2007 Capital Value rating valuation (less any land and dwelling insurance payments already made). The Crown will also take an assignment of all earthquake related insurance claims. There will be a process through which any property owners who consider that there is a material discrepancy between the 2007 rating valuation and the market value of their property (e.g. because of subsequent improvements) can raise their concerns; or.

1.1.2 **Option B:** The Crown will offer to purchase the land only at the greater of the following (less any EQC land payments already made):

1.1.2.1. 2007 Land Value rating valuation; or

1.1.2.2. EQC valuation for the minimum lot size applicable; and

1.1.3 The Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have.

Modification of package

2. **note** that there is some confusion about whether Option B (as outlined in recommendation 1.1.2) relates to both the land and the dwelling (i.e. the whole property) or the 'land only';

3. **agree** that the Option B package is reworded as the following:

3.1 The Crown will offer to purchase the property at the greater of the following (less any EQC land payments already made):

3.1.1 2007 Land Value rating valuation; or

3.1.2 EQC valuation for the minimum lot size applicable.

3.2 The Crown will also take an assignment of the EQC land claim, and landowners will be free to pursue their private insurance company for any other insurance claims they have.

4. **note** that in this and subsequent papers these options will be referred to as Option 1 and Option 2 respectively.

Purchase Option issues relating to Unit Title ownership

Unit titles – principal insurance policy held by body corporate

5. **note** that under a unit title scheme, the principal insurance policy is usually held by the body corporate and unless 75% of owners agree otherwise, proceeds of the principal policy must be applied to reinstatement.
6. **note** that under Option 1 if the Crown does not control at least 75% of the units and the votes, it will not be able to ensure that a special resolution in relation to the application of the proceeds of the principal insurance policy.
7. **note** that even where the Crown has 75% of the unit and votes it could still be subject to 'hold up' risk where owner(s) choose to stay in their unit(s) which would prevent the Crown demolishing the units it owns.
8. **note** that allowing individual unit owners to accept Option 1 of the Crown's offer will enable them to move on with their lives and provide them some future certainty.
9. **note** that Option 2 of the Crown's offer is not possible for unit titles unless all owners agree, as post sale individual owners do not retain an interest in the principal insurance policy as they are no longer a member of the body corporate.
10. **note** that under a unit title situation with a principal insurance policy held by the body corporate:
- 10.1 It is not possible for some owners to accept Option 1 and others to accept Option 2;
- 10.2 For Option 2 to be given practical effect, 100% of unit owners must agree to accept Option 2, with the body corporate's dwelling claims under the principal insurance policy being assigned to all of the owners jointly.
11. **agree** to allow individual unit owners to accept Option 1 of the Crown offer, but only allow Option 2 if all owners agree,
12. **note** recommendation 11 allows unit owners to accept at least one of the Crown's offers without the need to obtain their neighbours' consent.

Unit titles – individual insurance policies

13. **Note** that in some cases, unit title owners may have their own insurance policies, rather than a principal policy held by the body corporate.
14. **Agree** that in the case referred to in recommendation 13, Option 1 and 2 should be available to unit title holders, without requiring agreement from the other remaining owners.

Issues relating to Cross Leases Ownership

15. **note** that under a cross lease arrangement:
 - 15.1 the owners jointly own the land as tenants in common;
 - 15.2 Each individual owner is granted a lease of a specified proportion of the land
16. **note** that subject to anything to the contrary in the leases, the Crown will not be able to effectively to deal with the land unless it has acquired 100% of the interests of the owners.
17. **note** that cross lease properties can either have common walls or can be separate from one another.
18. **note** that under some cross lease arrangements owners have a joint insurance policy, in these cases unless all the owners assign their interests to the Crown, the Crown will not be able to progress an insurance claim.
19. **note** that under some cross lease arrangements owners have individual insurance claims 'split acceptances' of the Crown's offer could workable under this situation.
20. **note** that it will be more desirable for the Crown to have 100% acceptance of the owners of either Option 1 or Option 2. This will stop minority owners trying to delay or derail the process and it will enable the Crown to progress land or the building claims.
21. **note** the Crown could consider different rules for different insurance situations with cross lease ownership arrangements, whilst this would be more complex and costly to the Crown to complete the purchase transaction it will provide maximum flexibility to cross lease owners
22. **agree** to the either of the following options for Cross Leases:
 - o Have the same rules for all cross leased properties and allow individual cross lease owners to accept Option 1, but only allow Option 2 with an acceptance threshold of 100% of owners; or
 - o Have the same rules for all cross leased properties and offer cross lease owners both Options 1 and 2 with an acceptance threshold of 100% of owners (i.e. 100% must accept Option 1, or 100% must accept Option 2); or
 - o (preferred option): Have different rules for different types of cross leased properties:

- Individual cross lease owners may accept option 1
- If the cross leased properties have joint insurance, they may only accept option 2 if they all agree.
- If the cross leased properties have individual insurance, each may individually accept option 2.

Adjustments to purchase price due to incorrect 2007 rating valuation

23. Withheld under section 9(2)(g)(i)
24. Withheld under section 9(2)(f)(iv)
- 25.
26. **note** the Crown has made a offer that is based on pre-earthquake values and at a time when values were at the height of the property boom.
27. Withheld under section 9(2)(f)(iv) Withheld under section 9(2)(g)(i)
28. **note** that the purchase price is generous in that it is a value established pre-earthquake and by all accounts in a stronger property market. The true market value of the property post earthquake is dramatically less than the purchase price offered by the Crown.
29. Withheld under section 9(2)(f)(iv) Withheld under section 9(2)(g)(i)
30. **agree** it is not necessary to have any alternative valuation mechanism.
31. Withheld under section 9(2)(f)(iv) Withheld under section 9(2)(g)(i)
32. **agree** that if after an Option 2 offer is signed (including after settlement) the EQC valuation for the minimum lot size is for a higher value than the Land Value, that the government agrees to pay a "top-up".
33. **authorise** the Chief Executive of CERA to be given the discretion in the instance in recommendation 32 to determine the final purchase price and an appropriate date for the top-up option to conclude.

Property owners requesting Purchase Price Adjustments

34. **note** to provide certainty and simplicity the Crown adopted the 2007 Rating Valuations as the purchase price for insured residential properties within the Red Zones

The Crown seeking Purchase Price Adjustments For under insured properties

45. **note** a property is under insured if it is insured for a fixed sum or indemnity value which is less than the purchase price or insured for less than its actual floor area.
46. **note** adjusting for underinsurance means that the Crown is not incentivising inadequate insurance cover
47. **agree** to either of the following three options in relation to making adjustments to purchase price for under insured properties
 - reduce the purchase price on a pro rata basis relative to the percentage that the property is underinsured; OR
 - **(preferred option)** Where a property is under insured by more than 20% reduce the purchase price on a pro rata basis relative to the percentage that the property is underinsured; OR
 - Pay the property owner whose property was underinsured the full rating valuation.

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Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

The Crown seeking purchase price adjustments – for property owners who have already received insurance/EQC payments for reinstatement

51. **note** in some instances EQC and/or private insurance private insurance payments have been made to residential property owners and work has not been undertaken while other property owners in the Red Zone have spent this money on repair work
52. **note** property owners that have not spent payments on repair work are gaining a financial advantage over those who spent the money on repair work causing an inequity issue.
53. **note** that this will result in a high level of administrative low value deductions but the Crown will recoup payments made where the work has not been undertaken.
54. **agree** the method by which the Crown can make purchase price adjustments either:

- deduct from the purchase price any EQC and/or insurance payments already made, including emergency repairs except where the property owner has evidence that EQC and/or insurance payments have been spent on remediation works; OR
- (preferred option): only deduct from the purchase price reinstatement payouts and emergency repairs beyond 5% of the purchase price, except where the property owner has evidence that EQC and/or insurer payments have been spent on remediation works; OR
- make no adjustments to purchase price for unspent EQC/private insurance payouts made to property owners.

Chattels

55. **note** chattels are defined as blinds, curtains and or drapes, rugs, unfixed carpets, soft-wired (i.e. plug in) and freestanding (non-hardwired) stoves and lightshades;
56. **note** to include these in the Crown's purchase price would be simple and provide certainty to the offer;
57. **agree** to either that the purchase price is exclusive of chattels and the property owner can remove them before settlement.

Salvage Rights

58. **Agree**, in respect of Option 1, the property owner shall deal directly with the Crown's demolition contractor and in respect of Option 2, the property will need to deal directly with the insurer before settlement.

GST

59. **Agree** that the purchase price for the Red-Zone properties be rating valuation inclusive of GST, as property owners will either not be required to charge GST or the supply will be zero-rated for GST purposes.

Financial Recommendations

60. **Note** the financial implications relating to the recommendations in this paper are included in the companion Paper 2.

Next Steps

61. **invite** the Minister for Canterbury Earthquake Recovery to report to Cabinet in due course on any subsequent decisions that will be required on the treatment of commercial properties, and uninsured properties (including vacant lots) in the Red Zones.



Hon Gerry Brownlee
Minister for Canterbury Earthquake Recovery

15, 7, 14

Released by the Minister for Canterbury Earthquake Recovery