



Latest  
newsletter

September 2011 Newsletter

**The Future**

An interesting comment recently made by the CEO of Lumley Insurance, John Lyon was that “insurance will never be the same again”. Reflecting on the effects of the Canterbury earthquakes, Mr Lyon said that the entire Lumley normalised annual profit is now going to pay for reinsurance costs. The effects of this are already starting to be seen as increased rating structures flow through to insurance renewals.



**The Real Cost**

The true costs of Canterbury are now coming to light with the Reserve Bank providing some estimate of costs. The cost of residential claims is now estimated at \$9 billion, with commercial and infrastructure costs bringing the total to \$15 billion. This is equivalent to 8% of GDP.



An interesting comparison of the economic impact of the Canterbury disaster is shown in comparison with the Japanese earthquake that caused some \$35 billion in damage. The Japanese loss is the 2<sup>nd</sup> largest loss in history but in insurance premium terms represents only 6 months of premium in Japan whilst the Canterbury losses equate to more than 6 years of New Zealand premiums.

**Should We Have Known Of The Risk?**

As to whether we should have known of the possibility of an earthquake in Canterbury causing such wide damage is an interesting question with a now estimated 26,000 homes identified for demolition or rebuilding, and over 340,000 claims.

What is now known and is well documented is that in the 1880’s a large earthquake in Christchurch caused extensive liquefaction, but of course with the small population base at

that time, very little physical damage. Possibly as a result of this many homes in Christchurch today have “liquefaction risk” detailed on their property deeds and are commonly identified in LIM reports. Unfortunately, most people did not understand the terminology with many people believing that it referred to flood risk.



A clever clip capturing the extent of liquefaction. Click [here](#) to watch.

**Business Interruption – Indemnity Periods**

The woeful inadequacy of some business interruption, (loss of profits), policies and their indemnity periods has been brought to light following the Canterbury disaster. Some insureds have been found to have indemnity periods of only 6 months and in some, (fortunately few), cases, as low as 3 months.



## **Business Interruption – Indemnity Periods (cont.)**

The “usual” period is 12 months, however with many business’ especially those in the red zone not yet being able to access their premises means that with the 12 months anniversary of the first earthquake now upon us, their business interruption payouts will cease before they even have a chance to start rebuilding.

It is now recognised that whilst 12 months indemnity may be adequate for a single loss situation, (say a fire to a specific premises), the indemnity period needs to be considerably longer to cope with a situation such as an earthquake where there is widespread damage, code changes, aftershocks and prevention of access.

The industry is now promoting longer indemnity periods however this has inherent financial implications as earthquake rates have in most cases at least doubled, (in some areas in the Country even more), and acceptance of a 24 months indemnity period even at the old pre-earthquake rates doubles the premium. Thus even in a perceived low risk earthquake area, acceptance of 24 months indemnity period can result in a 400% increase in premium.

## **Leaky Homes**

The problem of leaky homes is still with us and has repercussions for the insurance industry. A Price Waterhouse Coopers report has estimated that there are 42,000 possible leaky homes in New Zealand. The estimated repair costs are \$13.3 billion.



Whilst these are large figures it is also felt that maybe only 10% of such homes will be actually identified as leaky and the Government scheme to assist repairs came into effect on 12 July 2011. Under this scheme Government foots 25% of the cost, the Local Authority another 25% with the balance being borne by the construction industry. In reality however many property owners will be out of pocket, with many builders no longer being in business, or houses being outside of the 10 year limit. It is estimated that some 80% of the homes are in the Auckland area.

## **Communication**

An interesting quote from WW2 Major-General “Windy” Gale:

“One purpose of communication is to take a thought from one human being’s brain and transmit it to the brain of others with the minimum possibility of misunderstanding, confusion or ambiguity”



An interesting observation as we as insurance brokers sometimes struggle to advise or inform clients of the terms imposed on them by their insurers, particularly at claim time.

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