EQC
EARTHQUAKE COMMISSION
KŌMIHANA RŪWHENUA

EARTHQUAKE COMMISSION
2009–2010 ANNUAL REPORT

Cover satellite imagery: Kevin Ward, NASA Earth Observatory

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Highlights

Catastrophe Response Programme

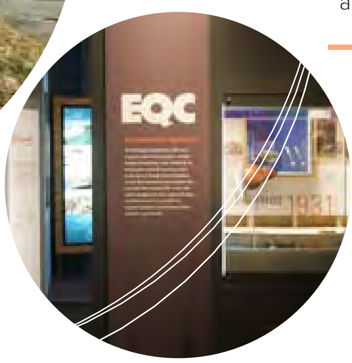
EQC support for new loss adjusters

The Commission has introduced a new scheme designed to increase the number of loss adjusters across New Zealand. This will ensure there are adequate numbers available to work for EQC following a major natural disaster. The scheme involves supporting the employment of trainee loss adjusters within major loss adjusting firms, over time creating a larger pool of loss adjusters on hand to work for EQC.

Natural Disaster Fund & Reinsurance

Natural Disaster Fund Growth

In another year of volatile investment markets, the Natural Disaster Fund grew by $355 million during the year. The increase of 6.4 percent saw the Fund reach $5.93 billion at balance date.



- Taupo volcanic seismic site
- Kiosk at *Awesome Forces*, Te Papa Tongarewa

Reinsurance Roll-Over

The reinsurance programme was successfully rolled over in an uncertain international market following severe storms in Europe, the Chile earthquake and hailstorms in Australia and America. Due to the increased number of insured houses, EQC's exposure grew by 1.85 percent for buildings and 1.94 percent for contents. Despite this, the cost of the reinsurance cover renewed this year fell by 2.2 percent compared to the same period last year.

Research & Public Education

GeoNet

In December the Board approved a further 10 years of funding for the national hazard monitoring network, GeoNet, designed and operated by the Crown Research Institute, GNS Science. This support will ensure that the high quality, real-time data that GeoNet supplies continues to expand and improve New Zealand's capacity to anticipate, mitigate and recover from major natural disasters.

Science-to-Practice Initiatives

EQC's Science-to-Practice programme fosters the delivery and uptake of science research. Notable initiatives undertaken this year included work with local government to improve planning in areas prone to landslip and work with the Department of Building and Housing to assist local government with the risk management of earthquake-prone buildings.

EQC kiosk

An exciting new EQC kiosk within the *Awesome Forces* exhibition at Te Papa shows the importance of preparing for natural disasters through both insurance and mitigation. EQC's messages are underscored in the stories of people affected by the recent Fiordland and Gisborne earthquakes, in a quake-safe computer game and in the sobering timeline of disasters that have struck these shores throughout our history.

Chairman's Report

A year ago, in my annual report as Chairman of EQC, I reflected on the turmoil in the international financial markets and the way in which EQC, as the custodian of the then $5.5 billion Natural Disaster Fund, had weathered the storms. 2009/10 had its own challenges but, by and large, global equity markets were more settled, and our investment managers more confident in their investment decisions on EQC's behalf.

This is shown in our financial results. Returns on global equities contributed $76 million to the Fund, even after losses in translation to New Zealand dollars (given the strength of our dollar over much of the year). Our Government stock holdings and other investment income contributed a further $310 million to the Fund, which, at 30 June, was just short of $6 billion.

FUND SIZE

How big should the Natural Disaster Fund be? To date, EQC's working assumption has been that, supported by a programme of reinsurance, it should be big enough to meet the cost of EQC's maximum probable liability – a magnitude 7.5 Wellington earthquake – and to rebuild within a reasonable time.

That translates into a $7 billion fund, supported by $2.5 billion of reinsurance. But EQC's operating environment is far from static and both this working assumption, and the fund size and structure that result from that assumption, warrant testing from time-to-time.

CHANGING RISK PROFILE

Claims incurred during 2009/10 totalled $20.8 million. Of that sum, more than $13 million was for land-related claims. It is an anomaly in the EQC scheme that homeowners pay a premium based on EQC cover of $100,000 for their dwelling and $20,000 for its contents, but coverage on land is uncapped. That has two important implications.

First, it is inequitable. A person whose house is situated on a high value section receives greater cover, at the same price, as the homeowner with a lower value section. Second, if severe weather events are to be a continuing feature of New Zealand's climate, the cost to EQC of landslips, storms and floods is likely to increase, with no corresponding premium adjustment.

By way of illustration, the average earthquake claim for the year was about $1,200; the average land claim was near $9,000.

Changing climate is only part of the context in which EQC operates. Science underpins our best estimates of the probability of a major Wellington earthquake, and its impact. As our knowledge of the geology and fault lines of the Wellington area increases, our estimates of the financial risk to EQC are further refined. The "It's Our Fault" project has resulted in a reduction in the probability of the major Wellington earthquake from 1-in-600 to 1-in-900 years. However further work on the subduction fault has yet to be factored in to this picture.

RISK TOLERANCE

Geology and climate are only two elements in EQC's operating context. The risk that the Government, as "owner" of EQC, is prepared to accept should, ideally, be verified from time-to-time. That risk has typically been couched as the likelihood of calling on the Crown Guarantee after the Natural Disaster Fund and our reinsurance cover have been exhausted. The Fund is now almost $6 billion, supported by $2.5 billion of reinsurance.

On paper, an $8.5 million buffer between a natural disaster and the Government having to provide funding seems a pretty safe bet. But as more than $4 billion of the Fund is in New Zealand Government securities, the Government will be faced with finding cash to redeem these once claims on EQC exceed around $4.3 billion. It may now be timely to look at a different balance between the Fund and reinsurance and, for the Fund itself, a different balance between New Zealand Government stock and other investments.

THE EQC TEAM

There have been changes in the Board during 2009/10. George Hooper and Garry Muriwai completed their terms as Board members. I thank them for their contribution. Denise Bovaird joined the Board in January. We are now a small Board of five Commissioners. I am grateful for their commitment and support to me as their Chairman.

In last year's annual report I referred to the decision of the then Chief Executive, David Middleton, to step down after 17 years in the role. In March this year Ian Simpson took up the position of Chief Executive EQC. He has already put his stamp on the organisation, building on the foundations established by his predecessor and the staff of the organisation. I take this opportunity to record my thanks to Ian, and to all the staff. EQC is a small organisation of 22 people, which does a big job for New Zealanders. It continues to be a privilege to be its chairman.

Michael Wintringham
Chairman

CANTERBURY EARTHQUAKE

This annual report for 2009/2010 had been signed off for printing when Canterbury was struck by a magnitude 7.1 earthquake on September 4, 2010.

For many people in Christchurch and the surrounding areas, this event will have a profound and lasting impact.

For the Earthquake Commission, it represents the greatest challenge the organisation has faced since its inception.

Not only is the Commission required to activate a network of specialist staff and contractors to respond to the nearly 100,000 claims lodged at the time of writing; we are part of a whole of Government response. Our own plans and processes will need to be sufficiently flexible and responsive to help meet the social, as well as the financial, aspects of the recovery.

The Earthquake Commission's Natural Disaster Fund, supported by its reinsurance contracts, can meet its share of the financial cost of rebuilding Canterbury. We are likely to be asked to do more, for example by taking direct responsibility for the physical repair and reconstruction of 50,000 damaged homes. We will do what is needed, to the best standard that we can achieve.

The Canterbury earthquake will test this country's preparedness for major natural disasters. For the Earthquake Commission, it will test the adequacy of our planning, and the effectiveness of our response. But more importantly, it will provide a basis on which to review the adequacy of New Zealand's institutional arrangements for natural disaster insurance, the role of EQC in those arrangements, and the size and structure of the Natural Disaster Fund. Those are matters for next year's annual report.

EQC's priority now is to help the Government provide certainty for those most affected by the earthquake, and play a constructive role in the social and physical rebuilding of Canterbury.

Michael Wintringham
Chairman

Chief Executive's Report

The unpredictable and inconstant nature of the risk EQC manages was underscored this year when just two events, one at the beginning and one at the end, generated 75 percent of our claims. The magnitude 7.8 Fiordland earthquake in July was one of the five largest earthquakes recorded anywhere in the world during the 12-month period, and the storms of May and June resulted in a number of serious landslips and widespread flooding.

Despite this, the claims volumes and costs were relatively modest. This was partly due to providence – had the Fiordland event been closer to a more densely populated area, EQC's costs would have been in the hundreds of millions if not billions of dollars. It was also because of New Zealand's high quality building standards and engineering. EQC's ongoing commitment to funding research and building close relationships with engineers, scientists and local authorities aims to further improve the physical resilience of New Zealand homes and workplaces.

The importance of this work was thrown into sharp relief by the events in Haiti in January and the following month in Chile. The magnitude 7.0 earthquake in Haiti released just one five-hundredth of the energy of the magnitude 8.8 event in Chile, yet resulted, horrifically, in 500 times the fatalities. The building standards in Chile share many similarities with those of New Zealand and, along with the immediate response from emergency services and civil defence groups, undoubtedly saved many thousands of lives.

EQC contributed to a New Zealand mission to Chile in the aftermath of the event to learn more about the economic and social impacts of the earthquake and its associated tsunami. The Commission remains in close contact with the Chilean authorities as their experiences of recovering from the earthquake and rebuilding the affected communities will be invaluable as we continue to improve our own Catastrophe Response Programme (CRP).

The findings of an independent review of the CRP, completed last year, have largely been implemented and confirmed our ability to manage an event which generates 30,000 to 60,000 claims. Our challenge is to ensure that we can manage a major catastrophe which generates over 150,000 claims, such as the Chile earthquake. This will involve co-ordination not just of the resources under EQC's direct control, but co-ordination on a national scale between government agencies, the construction industry and the insurance industry.

EQC also plays a key role in mitigating the economic consequences of a natural disaster through management of the Natural Disaster Fund and our global reinsurance programme.

The Fund has recovered well from the difficult markets over the past few years, delivering a return of 6.8 percent in line with market benchmarks. We continue to work closely with the other Crown Financial Institutions (CFIs), sharing experience and resources in areas such as responsible investing. More recently we have been working with the CFIs and Treasury to ensure consistent reporting of performance and risk.

The reinsurance programme was successfully rolled over in an uncertain international market. The first half of 2010 was amongst the most expensive first halves on record for the global insurance industry, with estimated insured losses from natural catastrophes of US$22 billion. Once again EQC's focus on long-term relationships and research investment paid dividends with premium rates dropping slightly on a risk-adjusted basis.

CLAIMS HANDLING AND CATASTROPHE RESPONSE

In total, EQC received 5,219 claims from the Fiordland quake, at a cost of $6.1 million. Four field support centres were set up to handle the claims, in Invercargill, Christchurch, Cromwell and Dunedin. EQC brought in 75 support people to work from these centres, settling 95 percent of claims by their closure in October.

The Commission also set up a support centre in Whakatane to help handle the 229 claims generated by the inundation of May and June. While the number of claims was relatively few, loss adjusters from outside the area were required to bolster local resources and ensure the claims were settled as quickly as possible.

In a new initiative, the Commission has introduced a scheme designed to increase the number of loss adjusters across New Zealand and, in turn, ensure there are adequate numbers available to work for EQC following a major natural disaster. The scheme involves supporting the employment of trainee loss adjusters within major loss adjusting firms for three-year periods. Each year a maximum of six such positions will be open to applicants. The successful candidates will be available to work for the Commission while they're training and, over time, there will be a larger pool of loss adjusters on hand to work for EQC.

ADMINISTRATION OF THE SCHEME

Private insurance companies collect premiums on EQC's behalf and the Commission carries out checks to ensure this happens accurately and expeditiously. The most important of these are external auditors' reports from each insurance company. The Commission received 10 reports from auditors during the year and all were unqualified.

RESEARCH

In December the Board approved a further 10 years of funding for the national hazard monitoring network, GeoNet, designed and operated by the Crown Research Institute, GNS Science. This support will ensure that the high quality, real-time data that GeoNet supplies continues to expand and improve New Zealand's capacity to anticipate, mitigate and recover from major natural disasters.

The Commission will provide $9 million p.a. for GeoNet for the next five years. Towards the end of this time funding for the second five years will be negotiated.

Since 2001, EQC's investment in GeoNet and related research has played a crucial role in recalibrating the risk models used by reinsurers to calculate EQC's reinsurance premiums. An NZIER report on the value of GeoNet found that the reduction in reinsurance costs relative to a business-as-usual projection has been equivalent to almost twice the value of this investment.

EQC also continues its support as lead stakeholder of the projects – "It's Our Fault" (Wellington seismic risk), and "DEVORA" (determining volcanic risk in Auckland).

In August three of EQC's four university programmes were renewed and co-funding for a new position at Massey University was agreed. Currently the Commission funds senior academic positions in earthquake engineering (University of Canterbury), hazards planning (Massey University), seismology (Victoria University) and volcano science and earthquake engineering (University of Auckland). The university positions contribute uniquely to New Zealand's capacity to develop and maintain knowledge and skills relevant to the assessment and mitigation of geological risk.

The new position of public education advisor, at the GNS-Massey Joint Centre for Disaster Research, aims to develop capability in social science to facilitate greater resilience to natural hazards.

PUBLIC EDUCATION

There were some exciting additions to the EQC-sponsored *Volcanoes* exhibition at the Auckland War Memorial Museum during the year. They included production of a new *Land on Fire* brochure and a comprehensive mini-website which was developed with the collaboration of Auckland University and GNS Science experts. With the first five-year sponsorship of the exhibition now concluded, the Commission and the museum have agreed terms for a new sponsorship. This will see the introduction of a dynamic multi-media show that will immerse the visitor within the region's volcanic landscape and complex climate as well as delivering EQC's messages.

There were also tremendous developments in the EQC-sponsored *Awesome Forces* exhibition at Te Papa. The most notable of these was the new EQC kiosk within the exhibition. The kiosk conveys the Commission's role in New Zealand's geological drama. It shows the importance of preparing for natural disasters through both insurance and mitigation – underscored in the stories of people affected by the recent Fiordland and Gisborne earthquakes, in a quake safe computer game and in the sobering timeline of disasters that have struck these shores throughout our history.

A three-year sponsorship of the Volcanic Activity Centre in Wairakei was renewed in January, continuing a relationship of 12 years. The Volcanic Activity Centre is a hands-on interactive educational centre, bringing the explosive past and present volcanic and geothermal features to life.

EQC's extensive work with schools continued this year. There was a virtual field trip to the Wellington Fault, a regional schools programme in Kapiti to complement the regional 'quake safe' pilot, and EQC-supported programmes at Te Papa and the Hawke's Bay Museum and Art Gallery.

MANAGING THE NATURAL DISASTER FUND

The Natural Disaster Fund grew by $355 million to $5.93 billion during the year, an increase of 6.4 percent over last year's total at balance date.

International share markets recovered quite strongly, although the rise in the value of the New Zealand dollar dampened the return to around 4 percent in New Zealand dollar terms.

After the deduction of management fees, EQC's active equity managers outperformed the MSCI world benchmark by 0.7 percent. The volatility in sharemarkets gave some of the active managers the opportunity to add value. There was no change to the Fund's structure and asset allocation during the year.

Reflecting generally weak economic conditions both locally and overseas, domestic short-term interest rates remained at very low levels, reducing EQC's cash returns. The Reserve Bank's Official Cash Rate was at a historic low of 2.5 percent for almost the entire year, only rising by 0.25 percent to 2.75 percent in June. As a consequence, bank deposits (RCDs) and Treasury bills produced low income during the year, with a combined return of 2.7 percent.

The average yield of New Zealand Government stock (NZGS) fell from 5.4 percent (30 June 2009) to 4.85 percent (30 June 2010), increasing the capital value of the bond portfolio. EQC's total returns for NZGS and inflation-indexed bonds, of a strong 7.9 percent and 9.9 percent respectively, were approximately in line with the indices.

Approximately 66 percent of EQC's portfolio is invested in NZGS and inflation-indexed bonds, and as at 30 June EQC held 9 percent of NZGS and 23 percent of inflation-indexed bonds on issue.

ASSET CLASS	ACTUAL RETURN	BENCHMARK/ TARGET RETURN
NZ Government stock	7.9%	8.2%
NZ Government inflation-indexed bonds	9.9%	9.9%
Bank bills (registered certificates of deposit)/Treasury bills	2.7%	2.5%
Passive global equities	4.1%	3.8%
Active global equities	4.5%	3.8%
Total Portfolio*	**6.8%**	**6.8%**

* The target return for the total portfolio is 1% plus the NZGS index return, over a rolling 10-year period. The structure has not been in place long enough to compare 10-year returns. For the five years to 30 June 2010, the actual portfolio return was 5.2% versus the target of 7.8%.

EQC's work with other Crown Financial Institutions ensures it has the resources and information necessary to engage effectively with investee companies on responsible investment matters and to fulfil EQC's obligation to avoid prejudice to New Zealand's reputation.

The Commission excludes from its investments companies engaged in the manufacture of cluster munitions, anti-personnel mines, nuclear weapons, and cigarettes and tobacco.

PEOPLE

I would like to thank my predecessor, David Middleton, for handing over the organisation in such great shape. Over his 17-year tenure EQC has become an international case study on how to manage a national catastrophe insurance scheme. His leadership and foresight, particularly in the areas of reinsurance, the CRP and research, have delivered significant value for EQC and for New Zealand.

In particular, I would like to thank the EQC team. They may be few in number but their passion, experience and ability to build effective partnerships nationally and internationally allow us to punch way above our weight. I feel privileged to have been given the opportunity to work with them as we take the next step in EQC's journey.

Ian Simpson
Chief Executive

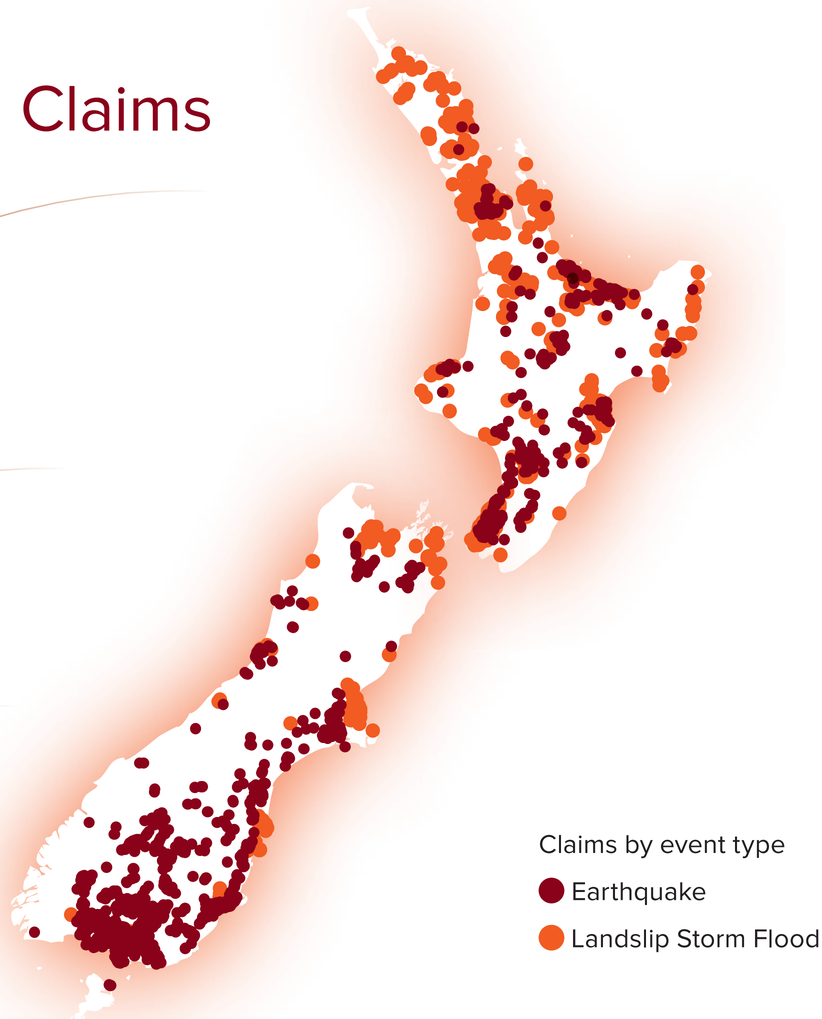
Natural Disaster Claims Locations

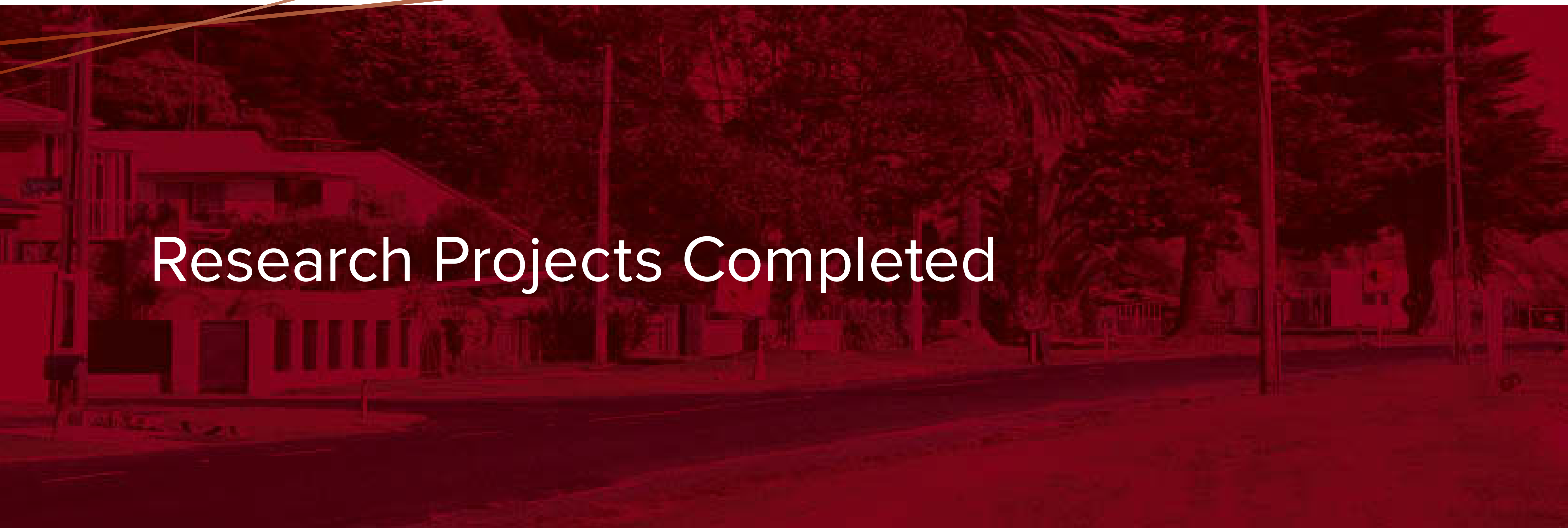
For claims incurred in the financial year

	2009-2010		2008-2009		AVERAGE OF PRIOR 5 YEARS	
	NO OF CLAIMS	PAYMENTS (000)	NO OF CLAIMS	PAYMENTS (000)	NO OF CLAIMS	PAYMENTS (000)
Earthquake	6,316	$7,442	2,265	$2,835	2,761	$7,145
Landslip	1,494	$13,342	2,226	$40,932	1,875	$28,802
Hydrothermal activity	2	$0	1	$0	2	$43
Volcanic eruption	0	$0	0	$0	0	$0
Tsunami	1	$0	0	$0	0	$0
Total	7,813	$20,784	4,492	$43,767	4,638	$35,990

Note: Financial statements disclose claims payments made and incurred in the financial year, so the figures are different from those in this table.

2009/2010 Claims





Research Projects Completed

Geomorphic hazards associated with glacial change, Aoraki/Mount Cook region, Southern Alps, New Zealand

S Allen – University of Canterbury
(EQC funded project 07/U538)

Slope stability and land use – Improving planning practice

Centre for Advanced Engineering New Zealand (CAENZ)
(EQC funded project 08/SP576)

Self-management of disaster risk and uncertainty: Evaluating a preventive health approach for building resistance to disaster

M Gowan – University of Canterbury
D Johnston, R Kirk – Massey University/GNS Science
K Ronan – Central Queensland University, Australia
(EQC funded project 08/UNI544)

Understanding a promising earthquake forecasting tool by computer modelling of seismicity

R Robinson, D Rhoades, M Gerstenberger – GNS Science
(EQC funded project 09/558)

Characterising the seismic potential of compressional inversion structures, NW South Island

R Sibson, F Ghisetti – University of Otago; TerraGeologica; University of Canterbury
(EQC funded project 08/547)

Quantifying the hazard from New Zealand's shallow intraslab earthquakes

M Reyners, D Eberhart-Phillips, J Ristau – GNS Science
(EQC funded project 08/549)

Post-disaster recovery of older adults

R Tuohy – GNS Science
(EQC funded project 09/U583)

Improving disaster preparedness of older adults living in the community

R Tuohy – GNS Science
(EQC funded project 09/U583)

Analysis and design of piles in liquefying soils

M Cubrinovski, J Haskell, B Bradley – University of Canterbury
(EQC funded project 08/545)

Characterisation of undrained behaviour of Christchurch soils – Phase 2

M Cubrinovski, S Rees – University of Canterbury
(EQC funded project 08/U574)

Ground-motion prediction models for post-earthquake rapid reporting and reliable loss modelling using a sparsely distributed recording network in New Zealand

J Zhao, M Gerstenberger – GNS Science
(EQC funded project 08/556)

Modelling visco-elastic source processes at Ngauruhoe Volcano, Central North Island, New Zealand

A Jolly, S Sherburn – GNS Science, Wairakei Research Centre
P Jousset – BRGM Orleans, France
P Smith, J Neuberg – University of Leeds, UK
(EQC funded project 08/552)

Earthquake response modelling for New Zealand very soft soil sites

U Destegul Solaroglu, G McVerry, J Zhao – GNS Science
(EQC funded project 08/554)

Tourism and Seismic Risk: Perceptions, preparedness and resilience in the zone of the Alpine Fault, Southern Alps, New Zealand

C Orchiston – University of Otago
(EQC funded project 07/U541)

Understanding the Holocene explosive eruption record of the Tongariro Volcanic Centre, New Zealand

A Moebis – Massey University
(EQC funded project 07/U542)

An investigation into the deformation behaviour of geosynthetic reinforced soil walls under seismic loading

P Jackson – University of Canterbury
(EQC funded project 08/U575)

Financial statements

AUDIT REPORT

To the readers of the Earthquake Commission's financial statements and statement of service performance for the year ended 30 June 2010.

The Auditor-General is the auditor of The Earthquake Commission (the Commission). The Auditor-General has appointed me, Ian C Marshall, using the staff and resources of Deloitte, to carry out the audit on her behalf. The audit covers the financial statements and statement of service performance included in the annual report of the Commission for the year ended 30 June 2010.

UNQUALIFIED OPINION

In our opinion:

- The financial statements of the Commission on pages 16 to 38:
  - › comply with generally accepted accounting practice in New Zealand; and
  - › fairly reflect:
    - the Commission's financial position as at 30 June 2010; and
    - the results of its operations and cash flows for the year ended on that date.
- The statement of service performance of the Commission on pages 39 to 44:
  - › complies with generally accepted accounting practice in New Zealand; and
  - › fairly reflects for each class of outputs:
    - its standards of delivery performance achieved, as compared with the forecast standards outlined in the statement of forecast service performance adopted at the start of the financial year; and
    - its actual revenue earned and output expenses incurred, as compared with the forecast revenues and output expenses outlined in the statement of forecast service performance adopted at the start of the financial year.

The audit was completed on 14 October 2010, and is the date at which our opinion is expressed.

The basis of our opinion is explained below. In addition, we outline the responsibilities of the Board and the Auditor, and explain our independence.

BASIS OF OPINION

We carried out the audit in accordance with the Auditor-General's Auditing Standards, which incorporate the New Zealand Auditing Standards.

We planned and performed the audit to obtain all the information and explanations we considered necessary in order to obtain reasonable assurance that the financial statements and statement of service performance did not have material misstatements, whether caused by fraud or error.

Material misstatements are differences or omissions of amounts and disclosures that would affect a reader's overall understanding of the financial statements and statement of service performance. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

The audit involved performing procedures to test the information presented in the financial statements and statement of service performance. We assessed the results of those procedures in forming our opinion.

Audit procedures generally include:

- determining whether significant financial and management controls are working and can be relied on to produce complete and accurate data;
- verifying samples of transactions and account balances;
- performing analyses to identify anomalies in the reported data;
- reviewing significant estimates and judgements made by the Board;
- confirming year-end balances;
- determining whether accounting policies are appropriate and consistently applied; and
- determining whether all financial statement and statement of service performance disclosures are adequate.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements and statement of service performance.

We evaluated the overall adequacy of the presentation of information in the financial statements and statement of service performance. We obtained all the information and explanations we required to support our opinion above.

RESPONSIBILITIES OF THE BOARD AND THE AUDITOR

The Board is responsible for preparing the financial statements and statement of service performance in accordance with generally accepted accounting practice in New Zealand. The financial statements must fairly reflect the financial position of the Commission as at 30 June 2010 and the results of its operations and cash flows for the year ended on that date. The statement of service performance must fairly reflect, for each class of outputs, the Commission's standards of delivery performance achieved and revenue earned and expenses incurred, as compared with the forecast standards, revenue and expenses adopted at the start of the financial year. The Board's responsibilities arise from the Crown Entities Act 2004 and the Earthquake Commission Act 1993.

We are responsible for expressing an independent opinion on the financial statements and statement of service performance and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001 and the Crown Entities Act 2004.

INDEPENDENCE

When carrying out the audit we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the New Zealand Institute of Chartered Accountants.

Other than the audit, we have performed additional assurance work over expenditure incurred in the processing of claims. Other than the audit, and this assignment, we have no relationship with or interests in the Commission.

Ian C Marshall
Deloitte

On behalf of the Auditor-General
Wellington, New Zealand

Statement of Comprehensive Income

FOR THE YEAR ENDED 30 JUNE 2010

	(NOTES)	ACTUAL 2010 $(000)	BUDGET 2010 $(000)	ACTUAL 2009 $(000)
Gross earned premiums	1	85,965	87,842	86,398
Outward reinsurance premium expense		(38,809)	(38,750)	(37,673)
NET EARNED PREMIUM REVENUE		**47,156**	**49,092**	**48,725**
Claims expense	2,3,5,13	(39,594)	(8,649)	(58,297)
Movement in unexpired risk liability	13	(6,000)	–	–
TOTAL UNDERWRITING COSTS		**(45,594)**	**(8,649)**	**(58,297)**
SURPLUS (DEFICIT) FROM UNDERWRITING ACTIVITIES		**1,562**	**40,443**	**(9,572)**
Public education		(2,381)	(3,054)	(2,708)
Research (excluding GeoNet)		(2,747)	(2,803)	(2,843)
GeoNet programme		(8,103)	(8,250)	(7,594)
TOTAL OTHER OPERATING COSTS		**(13,231)**	**(14,107)**	**(13,145)**
Investment income	4,5	385,518	326,351	76,795
Investment costs		(8,746)	(13,972)	(8,444)
INVESTMENT INCOME NET OF COSTS		**376,772**	**312,379**	**68,351**
Crown underwriting fee		(10,000)	(10,000)	(10,000)
NET SURPLUS FOR THE YEAR AND TOTAL COMPREHENSIVE INCOME		**355,103**	**328,715**	**35,634**

Statement of Movements in Equity

FOR THE YEAR ENDED 30 JUNE 2010

	(NOTES)	ACTUAL 2010 $(000)	BUDGET 2010 $(000)	ACTUAL 2009 $(000)
Natural Disaster Fund				
Capitalised reserves				
Opening balance at 1 July	6	1,500,000	1,500,000	1,500,000
Movement for the year		–	–	–
Closing balance at 30 June		1,500,000	1,500,000	1,500,000
Retained earnings				
Opening balance at 1 July		4,071,102	4,247,905	4,035,468
Net surplus for the year and total comprehensive income		355,103	328,715	35,634
Closing balance at 30 June		4,426,205	4,576,620	4,071,102
CLOSING BALANCE AS AT 30 JUNE		**5,926,205**	**6,076,620**	**5,571,102**

The Statement of Accounting Policies and Notes on pages 19 to 38 form part of and should be read in conjunction with these financial statements.

Statement of Financial Position

AS AT 30 JUNE 2010

	(NOTES)	ACTUAL 2010 $(000)	BUDGET 2010 $(000)	ACTUAL 2009 $(000)
Natural Disaster Fund				
Capitalised reserves	6	1,500,000	1,500,000	1,500,000
Retained surplus	6	4,426,205	4,576,620	4,071,102
TOTAL EQUITY		**5,926,205**	**6,076,620**	**5,571,102**
Assets				
Cash		11,209	10,739	9,392
Investments	5,9	5,973,608	6,120,445	5,612,613
Premiums receivable	7	18,364	17,000	17,434
Other receivables		189	–	–
Prepayments	8	6,725	6,574	6,405
Property, plant and equipment	10	14,828	14,697	14,232
Intangible assets	11	2,618	2,459	2,738
TOTAL ASSETS		**6,027,541**	**6,171,914**	**5,662,814**
Liabilities				
Trade and other payables	12	4,735	3,817	4,902
Provision for employee entitlements		210	177	216
Outstanding claims liability	13	11,845	15,593	8,901
Unearned premium liability	13	45,546	42,707	44,693
Unexpired risk liability	13	39,000	33,000	33,000
TOTAL LIABILITIES		**101,336**	**95,294**	**91,712**
NET ASSETS		**5,926,205**	**6,076,620**	**5,571,102**

The Statement of Accounting Policies and Notes on pages 19 to 38 form part of and should be read in conjunction with these financial statements.

Statement of Cash Flows

FOR THE YEAR ENDED 30 JUNE 2010

	(NOTES)	ACTUAL 2010 $(000)	BUDGET 2010 $(000)	ACTUAL 2009 $(000)
Cash flows from operating activities				
Cash was provided from:				
Premiums		85,698	87,842	86,821
Interest received		237,953	230,791	247,962
Dividends received		37,942	30,000	44,780
Net cash flow from GST		347	–	970
Cash was disbursed to:				
Outward reinsurance		(38,824)	(38,750)	(37,864)
Crown underwriting fee		(10,000)	(10,000)	(10,000)
Claims		(36,650)	–	(68,512)
Employees and other operating expenses		(11,860)	(25,753)	(11,901)
GeoNet operating expenses		(5,658)	(5,600)	(5,372)
Research grants		(2,059)	(2,195)	(2,352)
NET CASH INFLOW FROM OPERATING ACTIVITIES	20	**256,889**	**266,335**	**244,532**
Cash flows from investing activities				
Cash was provided from:				
Maturity and sales of investments		755,217	656,000	600,035
Disposal of property, plant and equipment		13	–	12
Cash was applied to:				
Purchase of investments		(1,006,590)	(916,441)	(843,977)
Purchase of property, plant and equipment	10	(3,454)	(3,370)	(3,689)
Purchase of intangibles	11	(258)	(250)	(504)
NET CASH OUTFLOW FROM INVESTING ACTIVITIES		**(255,072)**	**(264,061)**	**(248,123)**
NET INCREASE (DECREASE) IN CASH		**1,817**	**2,274**	**(3,591)**
Add opening cash brought forward		9,392	8,465	12,983
ENDING CASH CARRIED FORWARD		**11,209**	**10,739**	**9,392**

"Net cash flow from/to GST" represents the net GST paid to or received from the Inland Revenue Department. GST cash flow has been presented on a net basis as the gross amounts do not provide meaningful information for financial statement purposes.

The Statement of Accounting Policies and Notes on pages 19 to 38 form part of and should be read in conjunction with these financial statements.

Statement of accounting policies

FOR THE YEAR ENDED 30 JUNE 2010

Reporting Entity

The Earthquake Commission ("the Commission") is a Crown Entity as defined by the Crown Entities Act 2004 and is domiciled in New Zealand. The Commission's ultimate parent is the New Zealand Crown.

The Commission's primary objectives are to administer the insurance against natural disaster damage as provided for under the Earthquake Commission Act 1993, facilitate research and education about matters relevant to natural disaster damage, and to manage the Natural Disaster Fund including the arrangement of reinsurance. Accordingly, for purposes of New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS), it qualifies as a public benefit entity.

The reporting period covered by these financial statements is the year ended 30 June 2010. These accounts were approved by the Board on 2 September 2010.

Basis of Preparation

Measurement Base

The measurement base applied is historical cost modified by the revaluation of certain assets and liabilities as identified in this Statement of Accounting Policies.

Functional and Presentation Currency

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

Statement of Compliance

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

Judgements and Estimations

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

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

The estimation of claims liabilities is a key area of judgement where the assumptions made may have significant effect on the financial statements and estimates, with a significant risk of material adjustment in the next year. These are discussed in note 13.

Significant Accounting Policies

Insurance

Premium Income

Premium income is recognised using the 24ths rule to approximate the contract period over which the premiums are earned. Premiums not earned in the Statement of Comprehensive Income at balance date are disclosed in the Statement of Financial Position as unearned premiums. Premiums receivable are reported net of applicable discounts.

Insurance Recoveries

Reinsurance and non-reinsurance recoveries received or receivable are recognised as revenue in the Statement of Comprehensive Income.

Reinsurance

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

Claims

Claims expenditure includes claims settlements and claims handling costs.

Claims Liability and Unearned Premium Liability

The outstanding claims liability is recognised at balance date as the central estimate of the present value of the expected future payments for claims incurred to balance date, with an additional risk margin to allow for the inherent uncertainty in the central estimate.

At balance date, the Commission assesses the adequacy of the unearned premium liability. Where the current estimate of the present value of the expected future cash flows relating to future claims arising from the rights and obligations under current insurance contracts, plus an additional risk margin, exceeds the value of the unearned premium, the deficiency will be recognised in profit or loss and recorded in the Statement of Financial Position as unexpired risk liability.

Assets Backing Insurance Liabilities

All assets of the Commission back its insurance liabilities in accordance with section 13(3) of the Earthquake Commission Act 1993, which states: "All money in bank accounts established by the Commission, and all investments and other assets of the Commission, shall be deemed to form part of the Fund".

Grants

The Commission provides discretionary grants for earthquake research and research dissemination.

Discretionary grants are those where the Commission has no obligation to award on receipt of the grant application and are recognised as expenditure when the performance criteria, on which approval of the grant was based, are met.

Foreign Currency

Transactions in foreign currencies are initially translated at the foreign exchange rate at the date of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation, at year-end exchange rates, of monetary assets and liabilities denominated in foreign currencies, are recognised in the Statement of Comprehensive Income.

Taxation

The Commission is exempt from the payment of income tax in terms of the Income Tax Act 2004. Accordingly, no charge for income tax has been provided for.

Goods and Services Tax (GST)

The Statement of Comprehensive Income, Statement of Movements in Equity, Statement of Cash Flows, and commitments (note 17) are exclusive of GST. The Statement of Financial Position is also exclusive of GST, except for trade payables and premiums receivable, which are GST inclusive.

The amount of GST owing to or from the Inland Revenue Department at balance date, being the difference between output GST and input GST, is included in payables or receivables as appropriate.

Investments

Interest

Interest income is accrued using the effective interest rate method.

Dividends

Dividend income from investments is recognised when the Commission's rights as a shareholder to receive payment have been established.

Realised Gains and Losses

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

Unrealised Gains and Losses

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

Financial Instruments

Non-Derivative Financial Instruments

Non-derivative financial instruments comprise investments in equity and debt securities, premiums receivable, cash and trade and other payables.

Non-derivative financial instruments at fair value through profit or loss are recognised initially at fair value. Instruments not at fair value through profit or loss are recorded at fair value plus attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

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

Financial Instruments at Fair Value through Profit or Loss

An instrument is classified as at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through profit or loss if the Commission manages such instruments and makes purchase and sale decisions based on their fair value. Upon initial recognition, attributable transaction costs are recognised in profit or loss when incurred. Subsequent to initial recognition, financial instruments at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss.

Cash

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

Investments

All investment assets held by the Commission back insurance liabilities and are therefore designated at fair value through profit or loss.

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

Derivative Financial Instruments

The Commission uses derivative financial instruments to hedge its exposure to foreign exchange risks arising from investment activities. In accordance with its treasury policy, the Commission does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as trading instruments.

Derivative financial instruments are recognised initially at fair value, and transaction costs are expensed immediately. Subsequent to initial recognition, derivative financial instruments are stated at fair value. The gain or loss on re-measurement to fair value is recognised immediately in profit or loss.

Receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Receivables are recognised initially at fair value, being the present value of estimated future cash flows. They are subsequently measured at amortised cost using the effective interest rate method, less any impairment losses. Receivables with duration of less than 12 months are not discounted.

Impairment losses are assessed by an evaluation of the recoverable amount. The recoverable amount of the Commission's receivables carried at amortised cost is calculated as the present value of estimated future cash flows, discounted at the original effective interest rate (i.e. the effective interest rate computed at initial recognition of these financial assets). All individual receivables that are considered significant are subject to this approach. The impairment charge is recognised in the Statement of Comprehensive Income.

Other Financial Assets

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

Trade and Other Payables

Payables are non-derivative financial liabilities with fixed or determinable payments that are not quoted in an active market. Payables are recognised initially at fair value, being the present value of estimated future cash flows. They are subsequently measured at amortised cost using the effective interest rate method. Payables with duration of less than 12 months are not discounted.

Hedging

The Commission has not elected to apply hedge accounting to any derivatives for the year ending 30 June 2010.

Property, Plant and Equipment

Overview

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

Additions

The cost of an item of property plant and equipment is recognised as an asset only when it is probable that future economic benefits or service potential associated with the item will flow to the Commission and the cost of the item can be measured reliably.

Where an asset is acquired at no cost, or for a nominal cost, it is recognised at fair value when control over the asset is obtained.

Disposals

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount of the asset. Gains and losses are included in the Statement of Comprehensive Income.

Subsequent Costs

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

The costs of day-to-day servicing of property, plant and equipment are recognised in the Statement of Comprehensive Income as they are incurred.

GeoNet Assets

GNS Science administers the design, engineering, operation and maintenance of New Zealand's geological hazard monitoring system (GeoNet) under a 10-year agreement with the Commission. The services performed by GNS Science include the purchase, testing, installation and commissioning of capital equipment on behalf of the Commission.

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

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

Depreciation

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

Furniture and equipment	10 years
Leasehold improvements*	7–12 years
Motor vehicles	5 years
Computer and other electronic equipment	3 years
GeoNet buildings (mostly shelters)	25 years
GeoNet computer equipment	3 years
GeoNet equipment other than computer equipment	8 years

* The cost of leasehold improvements is capitalised and amortised over the unexpired period of the lease or the estimated remaining lives of the improvements, whichever is shorter.

Intangible Assets

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

Research and Development

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

Software Acquisition and Development

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

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

Intangible assets are amortised on a straight-line basis over the following useful lives:

Acquired computer software licences	1–3 years
Claims management system	7–9 years

Impairment of Non-Financial Assets

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

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in profit or loss.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell. Value in use is depreciated replacement cost for an asset where the future economic benefits or service potential of the asset are not primarily dependent on the asset's ability to generate net cash inflows and where the Commission would, if deprived of the asset, replace its remaining future economic benefits or service potential.

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

Leases

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

Liabilities

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

Employee Entitlements

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

Other Liabilities and Provisions

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

Contingent Liabilities

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

Changes in Accounting Policies

Accounting policies are changed only if the change is required by a standard or interpretation, or otherwise provides more reliable and more relevant information. There have been no accounting policy changes in the 2010 financial statements.

Commitments

Future payments are disclosed as commitments at the point a contractual obligation arises, to the extent that there are equally unperformed obligations.

Comparatives

When the presentation or classification of items in the financial statements is amended or accounting policies are changed voluntarily, comparative figures are restated to ensure consistency with the current period unless it is impracticable to do so.

Budgets

The budget figures are derived from the Statement of Intent as approved by the Board at the beginning of the financial year. The budget figures have been prepared in accordance with NZ IFRS, using accounting policies that are consistent with those adopted by the Commission for the preparation of the financial statements.

When presentation or classification of items in the financial statements is amended or accounting policies are changed voluntarily, budget figures are restated to ensure consistency with the current period unless it is impracticable to do so.

Superannuation Scheme

Defined Contribution Scheme

Obligations for contributions to the KiwiSaver and the State Sector Retirement Savings Scheme are accounted for as defined contribution superannuation schemes and are recognised as an expense in the Statement of Comprehensive Income as incurred.

Cost Allocation

Expenditure of the Commission is allocated across its four main functions: claims, research, education, and investment management. Expenditure is allocated to these functions by directly attributing costs as far as possible and by the apportioning of indirect costs based on the number of full time equivalents employed in each function.

Standards, Amendments and Interpretations Issued that are not yet effective and have not been early adopted

NZ IAS 24 'Related Party Disclosures' (revised 2009) replaces NZ IAS 24 'Related Party Disclosures' (issued 2004), and is effective for annual reporting periods beginning on or after 1 January 2011. The new standard removes the general disclosure exemption previously available to public benefit entities for transactions between entities subject to common Crown control transacted at arms' length. As a result, the Commission will be required to disclose the following information about such transactions:

(i) The nature and amount of each individually significant transaction; and

(ii) For other transactions that are collectively but not individually significant, a qualitative or quantitative indication of their extent.

The Commission intends to adopt this standard for the year ending 30 June 2012.

NZ IFRS 9 'Financial Instruments' issued 2009 is the first part of Phase 1 of the IASB's project to replace IAS 39 and is effective for reporting periods beginning on or after 1 January 2013. It addresses the classification and measurement of financial assets and requires all financial assets to be:

(a) classified on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial asset;

(b) initially measured at fair value plus, in the case of a financial asset not at fair value through profit or loss, particular transaction costs; and

(c) subsequently measured at amortised cost or fair value.

The requirements of NZ IFRS 9 are consistent with the policies currently applied by the Commission, and therefore the Commission expects no change in the measurement criteria of its financial assets. The Commission intends to adopt this standard for the year ending 30 June 2014.

Other standards and interpretations have been approved but are not yet effective, and are not expected to have a material impact on the Commission's financial statements.

Notes to the Financial Statements

FOR THE YEAR ENDED 30 JUNE 2010

1 PREMIUMS

	ACTUAL 2010 $(000)	BUDGET 2010 $(000)	ACTUAL 2009 $(000)
Gross premiums	89,029	90,118	88,905
Less discount	(2,211)	(2,276)	(2,218)
	86,818	**87,842**	**86,687**
Unearned premium opening	44,693	42,707	44,404
Unearned premium closing	(45,546)	(42,707)	(44,693)
	(853)	**–**	**(289)**
GROSS EARNED PREMIUMS	**85,965**	**87,842**	**86,398**

Premium income represents premiums collected and paid to the Commission by insurance companies and brokers. In accordance with Section 24 (2) of the Earthquake Commission Act 1993, the Commission receives declarations provided by insurance companies and brokers that all premiums collected have been returned to the Commission. It also contracts external auditors of insurance companies and brokers to review and report on those companies' internal controls and accounting systems so far as they are related to the Commission's premiums.

2 CLAIMS EXPENSE

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Current year	37,199	57,637
Prior years	2,395	660
	39,594	**58,297**

Current claims relate to risks borne in the current financial year. Prior years' claims adjustments arise when the actual number or value of claims settled differ from estimates at the previous year's balance date or from a re-assessment of the estimated liability for prior years' claims that remain unsettled at current balance date.

3 EXPENDITURE

	ACTUAL 2010 $(000)	BUDGET 2010 $(000)	ACTUAL 2009 $(000)
Advertising and publicity	1,240	1,460	1,061
Amortisation of intangibles	378	389	324
Fees to auditor			
Audit of the financial statements	90	87	86
Assurance services provided by auditor	10	14	18
Catastrophe Response Programme	4,680	5,763	5,157
Commissioners' fees	153	186	187
Depreciation	2,835	2,790	2,447
Employee remuneration and benefits	2,298	2,294	2,150
Grants for earthquake research	2,176	2,240	2,252
GNS Science GeoNet operating costs	5,402	5,600	5,263
Investment and custodial expenses – third party	7,434	12,597	7,205
Office rental	481	447	458
Sponsorships	630	1,040	1,103
Other	1,560	1,821	1,632
TOTAL OPERATING EXPENDITURE EXCLUDING REINSURANCE	**29,367**	**36,728**	**29,343**
Claims settlements and direct settlement costs*	**32,204**	**–**	**50,543**
TOTAL EXPENDITURE EXCLUDING REINSURANCE	**61,571**	**36,728**	**79,886**
Grouped by function per the Statement of Comprehensive Income			
Claims expense	39,594	8,649	58,297
Public education	2,381	3,054	2,708
Research (excluding GeoNet)	2,747	2,803	2,843
GeoNet Programme	8,103	8,250	7,594
Investment costs	8,746	13,972	8,444
	61,571	**36,728**	**79,886**

* The claims figure reported in the Statement of Comprehensive Income includes indirect claims administration costs and therefore differs from the claims settlements figure shown above. The Commission does not budget for the settlement of claims due to their unpredictable nature.

4 INVESTMENT INCOME

	ACTUAL 2010 $(000)	BUDGET* 2010 $(000)	ACTUAL 2009 $(000)
Global equities			
– Equity gains/(losses)	162,710	159,342	(529,167)
– Foreign exchange (losses)/gains	(124,691)	–	179,685
– Dividend income	37,836	–	45,333
	75,855	**159,342**	**(304,149)**
NZ Government stock			
– Price revaluation gains/(losses)	92,153	(41,344)	144,743
– Interest and discount income	208,697	199,638	213,765
	300,850	**158,294**	**358,508**
Other short-term investments			
– Interest income	8,813	8,715	22,436
INVESTMENT INCOME	**385,518**	**326,351**	**76,795**

* Budgeted investment income is based on projected medium term (5 year) asset returns.

5 MAJOR BUDGET VARIANCES

(a) Investment Income

Investment income exceeded budget this year due to an increase in New Zealand Government stock values as a result of a fall in average yields. While equity returns were better than budget in foreign currency terms, these gains were substantially offset by exchange losses due to the strong New Zealand dollar.

(b) Claims Expense

The budget provided only for the costs of operating the catastrophe response programme. However, claims costs for the year include those arising from the Fiordland earthquake of 17 July 2009 and landslips that occurred throughout the year.

(c) Investments

Investments are slightly lower than budgeted as the opening value of equity investments was substantially affected by the global credit crisis.

6 NATURAL DISASTER FUND

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
CAPITALISED RESERVES	**1,500,000**	**1,500,000**
Retained surplus		
Balance as at 1 July	4,071,102	4,035,468
Net surplus for the year and total comprehensive income	355,103	35,634
RETAINED SURPLUS AS AT 30 JUNE	**4,426,205**	**4,071,102**
CLOSING BALANCE OF THE NATURAL DISASTER FUND	**5,926,205**	**5,571,102**

Capitalised Reserves

1,500,000,000 ordinary shares of $1.00 each deemed to have been issued and paid up in full from the Fund on 1 October 1988.

Commission Solvency

The Commission has a contingent exposure to major disasters in excess of its current level of assets. In the event of the Commission's liabilities exceeding its assets (including reinsurance) the Crown, under Section 16 of the Earthquake Commission Act 1993, is obliged to provide, by way of grant or advance, sufficient funds to meet the shortfall.

Capital Management

The Natural Disaster Fund comprises retained surpluses and capitalised reserves. Equity is represented by net assets.

The Commission is subject to the financial management and accountability provisions of the Crown Entities Act 2004, which impose restrictions in relation to borrowings, acquisition of securities, issuing guarantees and indemnities and the use of derivatives.

The Commission manages its equity by prudently managing revenues, expenses, assets, liabilities, investments, and general financial dealings to ensure it effectively achieves its objectives and purpose, whilst remaining a going concern.

7 PREMIUMS RECEIVABLE

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Balance as at 30 June	**18,364**	**17,434**

Insurance companies and brokers are required to pay premiums within two months of the month in which they become payable in respect of residential policies. Premiums receivable represent these outstanding premiums.

All premiums are current, and the carrying amount of premiums receivable approximates fair value.

8 PREPAYMENTS

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Prepaid reinsurance asset as at 1 July	6,405	6,106
Deferral of reinsurance premiums on contracts entered during the period	6,725	6,405
Earnings of reinsurance premiums on contracts entered into during previous periods	(6,405)	(6,106)
PREPAID REINSURANCE AS AT 30 JUNE	**6,725**	**6,405**

Premiums on reinsurance contracts are paid three months in advance and are released to the Statement of Comprehensive Income from the date of attachment in accordance with the expected pattern of risk.

9 FINANCIAL INSTRUMENTS

Section 12 of the Earthquake Commission Act 1993 and Section 103 of the Crown Entities Act 2004 give the Minister of Finance authority to issue directions to the Commission.

A direction from the Minister of Finance was issued on 1 November 2001 permitting investments to be held in New Zealand Government securities (New Zealand Government stock, inflation-indexed stock and Treasury bills), New Zealand bank securities (maximum $250 million) and global equities up to a maximum of 35% of total investments. All investments in New Zealand Government securities are issued by the Reserve Bank and are only tradable with the New Zealand Debt Management Office (NZDMO).

At 30 June 2010 the fair values and concentrations of the Commission's investments were as follows:

	2010 FAIR VALUE $(000)	2010 % OF TOTAL INVESTMENT	2009 FAIR VALUE $(000)	2009 % OF TOTAL INVESTMENT
NZ Government stock	3,427,541	57.4%	3,240,375	57.7%
NZ Government inflation-indexed stock	537,413	9.0%	509,038	9.1%
NZ Government Treasury bills	174,266	2.9%	4,989	0.1%
TOTAL GOVERNMENT SECURITIES	**4,139,220**	**69.3%**	**3,754,402**	**66.9%**
NZ BANK SECURITIES	**149,423**	**2.5%**	**249,094**	**4.4%**
Global equities – active	1,012,494	16.9%	963,127	17.2%
Global equities – passive	672,471	11.3%	645,990	11.5%
TOTAL GLOBAL EQUITIES	**1,684,965**	**28.2%**	**1,609,117**	**28.7%**
TOTAL INVESTMENTS	**5,973,608**	**100.0%**	**5,612,613**	**100.0%**
Current	323,689	5.5%	927,320	16.5%
Non-current	5,649,919	94.5%	4,685,293	83.5%
	5,973,608	**100.0%**	**5,612,613**	**100.0%**

Interest Rate Risk

Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The Commission's investments in Government stock, Treasury bills and New Zealand bank securities expose it to interest rate risk.

The Commission passively manages its Government stock portfolio. This means that the portfolio is exposed to an interest rate risk identical to the New Zealand Government stock index.

In the event of a major catastrophe, the NZDMO has agreed to buy back the Commission's Government stock at pre-catastrophe prices.

The Commission's investments have the following average market yields and durations:

	2010 YIELD	DURATION	2009 YIELD	DURATION
NZ Government stock	4.52%	4.14 yrs	4.45%	3.39 yrs
NZ Government inflation-indexed stock	2.47%	5.12 yrs	3.34%	5.90 yrs
NZ Government Treasury bills	2.55%	59 days	2.59%	31 days
NZ Bank Securities	2.95%	47 days	2.75%	47 days

Fair Value Interest Rate Risk Sensitivity

A 50 basis point increase in interest rates would decrease the surplus at balance date by $81,774,509 (2009: $67,280,839). A 50 basis point decrease would increase the surplus by $84,411,524 (2009: $69,350,554).

Cash Flow Interest Rate Risk

The Commission does not invest in variable rate instruments, and is therefore not subject to cash flow interest rate risk.

Global Equities' Market Price Risk

The Commission is exposed to price volatility and exchange rate fluctuations on its global equity investments.

Managing market pricing risks associated with global equities is achieved by maintaining a tracking error against the benchmark index of not more than 0.5% per annum for passive investments. Active global equity managers are allowed a larger tracking error, but are subject to other constraints. These include their aggregated individual company exposures being limited to 5% of funds invested in global equities, investment restricted to 5% of a company's market capitalisation, and restrictions on industry and country exposures (including a restriction on the country universe) to limit sector over-exposure. Holdings in illiquid securities are restricted or prohibited. The multi-manager style also enables a diversification of risk.

The fair values of equity investments are determined by reference to published price quotations on the world markets.

The Commission does not currently hedge currency translation exposures arising through investments in global equities as global equities will only be liquidated when the Commission is faced with a major natural disaster. At the time this policy was adopted, both the Reserve Bank and the Commission's investment advisers were of the opinion that in such an event the most likely scenario is for the New Zealand dollar to depreciate and inflation to rise. This would result in an increase in the Commission's liabilities but also an increase in the value of the Commission's un-hedged global investments.

The Commission's global equity investments are concentrated in the following currencies:

	2010	2009
EURO	15%	17%
GBP	10%	10%
USD	51%	49%
JPY	9%	10%
Other	15%	14%
	100%	**100%**

Price Risk Sensitivity

A 5% increase in the value of the New Zealand dollar at balance date would reduce the surplus by $80,236,433 (2009: $76,624,610). A 5% decrease in the value would increase the surplus by $88,682,373 (2009: $84,690,358).

A 5% increase in the MSCI World index at balance date would increase the surplus by $84,248,254 (2009: $80,445,840). A 5% decrease in the index would reduce the surplus by $84,248,254 (2009: $80,455,840).

Credit Risk

The Commission is exposed to the credit risk of a bank defaulting on an investment. The Commission reduces credit risk by investing funds only in securities issued by approved New Zealand banks that have a short-term credit rating of A-1 or higher from Standard and Poor's. Exposure to any one bank with a rating of less than A-1+ is restricted to a maximum of 15% of total bank securities, but for banks with a rating of A-1+, the exposure may be extended to 25%. No collateral is held by the Commission in respect of bank balances or short-term securities due to the credit rating of financial institutions with whom the Commission transacts business. At balance date the Commission held short-term securities with five registered banks. The maximum exposure at balance date was $149,426,817 (2009: $249,071,700).

Liquidity Risk

The Commission's financial liabilities consist of claims payable and other trade payables. It is expected that all claims and trade payables outstanding at balance date will be settled within 12 months (2009: 12 months).

The Commission's liquidity risk is the risk of having insufficient liquid funds available to meet claims and trade and other payables as they fall due. To manage this risk, the Commission retains a cash allocation of 7% of investments. Cash is invested in either bank securities or Treasury bills for periods up to 92 days. Bank securities maturity dates are spread to ensure that at least $50 million is available each month to meet operational requirements.

All other investments are highly liquid and can be sold in a relatively short time-frame to meet any operational requirements.

The average durations until maturity are shown earlier in this note.

10 PROPERTY, PLANT AND EQUIPMENT AND DEPRECIATION

	PLANT & EQUIPMENT $(000)	GEONET BUILDINGS $(000)	GEONET COMPUTER EQUIPMENT $(000)	GEONET OTHER EQUIPMENT $(000)	TOTAL PROPERTY PLANT & EQUIPMENT $(000)
2010					
Cost					
At 1 July 2009	1,200	862	1,609	20,590	24,261
Additions	113	499	323	2,519	3,454
Disposals	(113)	–	(37)	(54)	(204)
At 30 June 2010	1,200	1,361	1,895	23,055	27,511
Accumulated depreciation					
At 1 July 2009	828	46	1,187	7,968	10,029
Depreciation charge	146	72	205	2,412	2,835
Disposals	(103)	–	(37)	(41)	(181)
At 30 June 2010	871	118	1,355	10,339	12,683
CARRYING AMOUNTS AT 30 JUNE 2010	**329**	**1,243**	**540**	**12,716**	**14,828**
2009					
Cost					
At 1 July 2008	1,196	454	1,419	17,779	20,848
Additions	163	408	279	2,839	3,689
Disposals	(159)	–	(89)	(28)	(276)
At 30 June 2009	1,200	862	1,609	20,590	24,261
Accumulated Depreciation					
At 1 July 2008	832	18	1,059	5,910	7,819
Depreciation charge	139	28	208	2,072	2,447
Disposals	(143)	–	(80)	(14)	(237)
At 30 June 2009	828	46	1,187	7,968	10,029
CARRYING AMOUNTS AT 30 JUNE 2009	**372**	**816**	**422**	**12,622**	**14,232**

11 INTANGIBLE ASSETS

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Computer software		
Cost		
At 1 July	3,160	2,656
Additions	258	504
Disposals	–	–
At 30 June	3,418	3,160
Accumulated Amortisation		
At 1 July	422	98
Depreciation charge	378	324
Disposals	–	–
At 30 June	800	422
CARRYING AMOUNT 30 JUNE	**2,618**	**2,738**

12 TRADE AND OTHER PAYABLES

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Trade payables	257	1,058
Tax on reinsurance	1,335	1,356
GST payable	640	293
Accruals	2,503	2,195
	4,735	**4,902**

Trade and other payables are non-interest bearing and are normally settled on 30-day terms, therefore the carrying value of trade and other payables approximates their fair value.

13 CLAIMS LIABILITIES

The Commission covers the following types of hazard: earthquake, natural landslip, volcanic eruption, hydrothermal activity and tsunami, as well as fire caused by any of the above. There is generally no significant delay between the occurrence of such events and the reporting of claims, and claims are usually settled within 12 months of being reported.

At balance date, the Commission recognises a liability in respect of outstanding claims, including amounts in relation to unpaid reported claims, claims incurred but not reported (IBNR), claims incurred but not enough reported (IBNER) and costs including claims handling costs. The Commission also assesses the adequacy of the unearned premium liability.

The Earthquake Commission Act 1993 requires all claims to be reported within three months of an event, and given the reporting time-frame from balance date, the key area of estimation risk is therefore IBNER. The volatility of IBNER is partially mitigated by the maximum settlement amounts of $20,000 for personal property and $100,000 for dwellings. However, claims in relation to residential land are not subject to a monetary limit and are therefore subject to greater volatility.

Actuarial calculations were not performed with respect to outstanding claims at June 2010 as the number and total value of outstanding claims at balance date was very low. Accordingly it was considered that the benefit of calculating actuarial adjustments would not justify the cost, as such adjustments would be immaterial.

Outstanding Claims Liability

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Outstanding claims liability		
Central estimate of claims reported at balance date	10,330	7,271
Claims handling costs	1,070	1,295
Risk margin	445	335
GROSS OUTSTANDING CLAIMS LIABILITY	**11,845**	**8,901**
Current	11,366	7,556
Non-current	479	1,345
	11,845	**8,901**
Risk margins applied	3.9%	3.9%
Reconciliation of movement in outstanding claims liability		
Outstanding claims liability at 1 July	8,901	19,116
Add claims expense recognised in the Statement of Comprehensive Income	39,594	58,297
Less claims payments during the year	(36,650)	(68,512)
OUTSTANDING CLAIMS LIABILITY AT 30 JUNE	**11,845**	**8,901**

The risk margin adopted by the Commission is intended to secure an adequacy level of 75%, which is the minimum level required by the Australian Prudential Regulations Authority, Prudential Standard GPS 210.

No discount factor or inflation factor was applied to the calculation as claims are generally settled within one year.

Unearned Premium Liability and Unexpired Risk Liability

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Unearned premium liability		
Unearned premium liability at 1 July	44,693	44,404
Deferral of premiums on contracts written in the period	45,546	44,693
Earning of premiums written in previous periods	(44,693)	(44,404)
UNEARNED PREMIUM LIABILITY AT 30 JUNE	**45,546**	**44,693**

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Unexpired risk liability		
Unexpired risk liability balance at 1 July	33,000	33,000
Movement for the year	6,000	–
UNEXPIRED RISK LIABILITY AT 30 JUNE	**39,000**	**33,000**

The actuarial estimate for the unearned liabilities was reviewed in the 2010 year by Melville Jessup Weaver, led by Janet Lockett, a Fellow of the New Zealand Society of Actuaries. In determining the actuarial estimate, the actuary relied upon information supplied by the Commission and was satisfied as to the nature, sufficiency and accuracy of the information provided. As a result of this review an adjustment was made as calculated below.

Legislation recognises that EQC's premiums may be inadequate to meet its liabilities in any one year by enabling it to set aside any annual surplus free of tax in the Natural Disaster Fund and, in the case of a very severe catastrophe (that exceeds both the Fund and reinsurance recoveries) by providing for a Crown Guarantee. The Commission currently has the capability to cover a 1-in-1000-year event with an estimated value of up to $8.4 billion before having to call on the Crown Guarantee.

Whilst the ability of EQC to meet its claims liabilities is therefore in no doubt, the Commission is required to perform a liability adequacy test to determine whether the carrying amount of the unearned premium liability is sufficient to cover estimated future claims relating to existing contracts.

This test and the resulting liability adjustment are performed solely to ensure compliance with NZ IFRS 4 – *Insurance Contracts*. As this standard is intended for general insurers and does not provide for the Commission's unique circumstances, the result should not be read as an accurate indicator of the adequacy of its premiums.

The liability adequacy calculation is based on the central estimate of the costs expected to arise annually from minor events, obtained from historical data, plus a risk margin intended to lift this to a level approximating 75% adequacy. Added to this is an amount equivalent to the central estimate of the potential future outcomes from earthquake events costing greater than $50 million and extending to very severe but extremely rare events, taking into account the projected frequencies at which such events may occur.

An unexpired risk liability of $39 million was determined at 30 June 2010, calculated as follows:

		2010 $(000)
Unexpired risk liability		
Calculation of deficiency		
Unearned premium liability		45,546
Central estimate of present value of expected future cash flows arising from future claims on general contracts issued	(85,100)	
Risk margin	(7,500)	
Gross deficiency		(92,600)
Present value of expected future cash inflows arising from reinsurance recoveries on future claims on general contracts issued		8,000
NET DEFICIENCY		**(39,054)**

14 INSURANCE RISKS

The Commission must accept exposure to claims for the natural catastrophes as specified in the Earthquake Commission Act 1993 and therefore may not seek to reduce its claims exposure by diversification of its business over classes of insurance or geographical region. The premium level is set by the Earthquake Commission Regulations 1993 and does not differentiate between risk types, nor is it adjusted in response to the level of claims expected or incurred.

Reinsurance Programme

The Commission limits its exposure to a very large-scale natural disaster through the purchase of reinsurance with the objectives of:

+ Minimising the overall cost to secure mandated protection to New Zealand homeowners;
+ Implementing a reinsurance programme that provides stability over time against reasonably foreseeable events;
+ Providing flexibility in the reinsurance agreement terms and conditions should the Crown determine a different risk profile under the natural disaster insurance scheme; and
+ Minimising the risk of default amongst reinsurers by limiting its exposure to any one reinsurer or related group of reinsurers, and by applying the following policies:

  (i) Setting a target for the overall programme at placement that achieves an average score (weighted by signed-line aggregates) of Standard & Poor's (S&P) financial strength rating of A or better.

  (ii) Normally placing reinsurance with organisations who have the following security ratings:
  S&P – AAA to A- (i.e. from "extremely strong" to "strong")
  Best's – A++ to A- (i.e. from "superior" to "excellent").

  (iii) Diligent examination by EQC management of the case for inclusion of a non-complying reinsurer, with the assistance of its reinsurance broker, and obtaining Board approval of any decision to include such reinsurers.

Crown Underwriting Fee

It is recognised that the Fund plus reinsurances may not be sufficient to cover claims arising from a major urban catastrophe and/or other losses and costs. In those events the Crown would be called upon to meet any shortfall, under Section 16 of the Earthquake Commission Act 1993. This states: "If the assets of the Commission (including the money for the time being in the Fund) are not sufficient to meet the liabilities of the Commission, the Minister of Finance shall, without further appropriation than this section, provide to the Commission out of public money such sums by way of grant or advance as may be necessary to meet the deficiency upon such terms and conditions as the Minister of Finance determines."

Pursuant to Section 17 of the Earthquake Commission Act 1993, the Commission is required to pay fees to the Crown as determined by the Minister of Finance. The Minister of Finance has determined that $10 million be paid for the year ended 30 June 2010 (2009: $10 million).

Interest Rate and Credit Risk

No direct exposure to interest rate risk results from the financial assets or liabilities arising from insurance or reinsurance contracts. Financial assets and liabilities arising from insurance or reinsurance contracts are stated in the Statement of Financial Position at the amount that best represents the maximum credit risk exposure at balance date. There are no significant concentrations of credit risk.

Research and Education

The Commission seeks to indirectly reduce the extent of claims incurred, by the dissemination of research and through public education programmes.

15 CONTINGENT LIABILITIES AND ASSETS

There were no contingent assets or liabilities at June 2010 (2009: nil).

16 CATEGORIES OF FINANCIAL ASSETS AND LIABILITIES

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Financial assets at fair value through profit or loss		
Government securities	4,139,220	3,754,402
New Zealand bank securities	149,423	249,094
Global equities	1,684,965	1,609,117
	5,973,608	**5,612,613**
Loans and receivables		
Cash	11,209	9,392
Premiums receivable	18,364	17,434
Other receivables	189	–
	29,762	**26,826**
Financial liabilities measured at amortised cost		
Trade and other payables	(4,735)	(4,902)
Provision for employee entitlements	(210)	(216)
Outstanding claims liability	(11,845)	(8,901)
	(16,790)	**(14,019)**

FAIR VALUE

Financial instruments that are measured subsequent to initial recognition at fair value are grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

All of the Commission's financial instruments are classified within level 1.

17 COMMITMENTS

ClaimCenter Services Contract

In 2007, the Commission entered into a services contract for the provision of a computer system for claims handling, processing and allocation.

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Operating Commitment		
(a) Not later than one year	1,959	1,921
(b) Later than one year and not later than two years	1,959	1,921
(c) Later than two years but not later than five years	5,878	5,762
(d) Later than five years	3,265	5,122
TOTAL CLAIMCENTER COMMITMENT	**13,061**	**14,726**

Reinsurance Contracts

The Commission has signed contracts for reinsurance in the international market. The contracts are for terms ranging from one year to three years.

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Operating Commitment		
(a) Not later than one year	38,455	38,403
(b) Later than one year and not later than two years	21,301	23,186
(c) Later than two years but not later than five years	6,544	12,432
(d) Later than five years	–	–
TOTAL REINSURANCE COMMITMENTS	**66,300**	**74,021**

GNS Science

The Commission has a contract with GNS Science for the development and implementation of a seismic monitoring and reporting network (GeoNet). As the current contract expires in 2011, a new contract was signed during the year, which covers the years from 2012 to 2021.

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Capital Commitment		
(a) Not later than one year	3,426	3,170
(b) Later than one year and not later than two years	3,498	3,747
(c) Later than two years but not later than five years	10,060	–
(d) Later than five years	19,283	–
Operating Commitment		
(a) Not later than one year	5,512	5,600
(b) Later than one year and not later than two years	5,580	5,572
(c) Later than two years but not later than five years	17,389	–
(d) Later than five years	37,804	–
TOTAL GNS SCIENCE COMMITMENTS	**102,552**	**18,089**

Te Papa Tongarewa, Museum of New Zealand

In 2008, the Commission signed a contract with Te Papa for sponsorship. The sponsorship relationship is linked to the *Awesome Forces* and *Quake Braker* exhibitions at Te Papa, which provide a mechanism to communicate the Commission's key messages to a broad audience and meet its educational and research objectives.

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Operating Commitment		
(a) Not later than one year	500	500
(b) Later than one year and not later than two years	500	500
(c) Later than two years but not later than five years	–	500
(d) Later than five years	–	–
TOTAL TE PAPA TONGAREWA, MUSEUM OF NEW ZEALAND COMMITMENT	**1,000**	**1,500**

Research Grants

Future research grants approved by the Board.

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Operating Commitment		
(a) Not later than one year	1,832	1,142
(b) Later than one year and not later than two years	1,070	675
(c) Later than two years but not later than five years	1,290	300
(d) Later than five years	8	–
TOTAL RESEARCH GRANT COMMITMENTS	**4,200**	**2,117**

Building Leases

The Commission has a non-cancellable long-term lease on premises in Wellington. The annual lease payments are subject to three-yearly reviews. The amounts disclosed below as future commitments are based on the current rental rates.

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Operating Commitment		
(a) Not later than one year	494	508
(b) Later than one year and not later than two years	494	508
(c) Later than two years but not later than five years	1,481	1,524
(d) Later than five years	948	1,482
TOTAL BUILDING LEASE COMMITMENT	**3,417**	**4,022**

Claims Management Services

The Commission has an agreement with Gallagher Bassett Services Pty Ltd for the provision of claims management services which finished in 2010. This agreement has been extended for a further year.

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Operating Commitment		
(a) Not later than one year	906	870
(b) Later than one year and not later than two years	–	–
(c) Later than two years but not later than five years	–	–
(d) Later than five years	–	–
TOTAL CLAIMS MANAGEMENT SERVICES COMMITMENT	**906**	**870**

18 RELATED PARTY TRANSACTIONS

The Earthquake Commission is a Crown Entity of the New Zealand Government and all significant transactions with the Crown result from Ministerial directions given under the Earthquake Commission Act 1993 or Section 103 of the Crown Entities Act 2004.

The Commission enters into numerous transactions with other Crown agencies, tertiary institutions and state-owned enterprises on an arm's-length basis. Where those parties are acting in the course of their normal dealings with the Commission, related party disclosures have not been made for transactions of this nature.

Information on significant related party transactions with GNS Science (GeoNet Project) and the Crown underwriting fee are reported separately within the financial statements and the accompanying notes.

During the year, the Commission received services from a company whose directors are close relatives of key management personnel. Payments for services in 2010 totalled $4,781 (2009: $73,817). The terms and conditions of this contract are no more favourable than the Commission would have adopted if there were no relationship to key management personnel. The contract with this party ceased in 2009.

Key Management Personnel Compensation

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Salaries and other short-term employee benefits	**1,026**	**1,007**

Key management personnel for the 2010 and 2009 years include all Commissioners, the Chief Executive and three senior managers.

19 DISCLOSURES

Employee Remuneration

The number of employees whose total remuneration for the financial year was in excess of $100,000, in $10,000 bands, are as follows:

$(000)	2010	2009
100–110	1	
110–120	2	2
120–130		1
130–140	2	
160–170	2	1
170–180		1
190–200	1	
200–210		1
240–250	1	
280–290		1

The outgoing Chief Executive resigned from his position effective 28 February 2010. Total remuneration paid to that date was in the $240,000–$250,000 band (2009: $280,000–$290,000 band). The incoming Chief Executive commenced on 1 March 2010 and total remuneration paid from this date until 30 June 2010 was in the $90,000–$100,000 band.

Commissioners' Remuneration

Commissioners' fees paid during the year were as follows:

	FEES – 2010 ($)	FEES – 2009 ($)
MC Wintringham	46,400	46,400
KB Taylor (i)	29,000	24,167
TP McGuinness (ii)	–	2,513
CB Durbin (iii)	–	19,333
RJ Hooper (iv)	5,800	23,200
WN Hoadley (v)	1,933	23,200
GT Muriwai (vi)	11,600	23,200
L Robertson (vii)	23,200	21,267
G McLachlan (viii)	23,200	3,867
D Bovaird (ix)	11,600	–
TOTAL	**152,733**	**187,147**

No additional remuneration was paid to Commissioners.

(i) Appointed as Deputy Chairman 1 May 2009

(ii) Term concluded 9 August 2008

(iii) Term concluded 30 April 2009

(iv) Term concluded 30 September 2009

(v) Term concluded 31 July 2009

(vi) Term concluded 1 January 2010

(vii) Appointed to Board 10 August 2008

(viii) Appointed to Board 1 May 2009

(ix) Appointed to Board 1 January 2010

Indemnity and Insurance Disclosure

The Commission has provided a deed of indemnity to each Board member in relation to certain activities undertaken in the performance or intended performance of Commission's functions.

The Commission effected and maintained "Directors and Officers Liability" and "Professional Indemnity" insurance cover during the financial year, in respect of the liability or costs of any Board member, or employee.

20 RECONCILIATION OF OPERATING SURPLUS TO NET CASH FLOW FROM OPERATING ACTIVITIES

	ACTUAL 2010 $(000)	ACTUAL 2009 $(000)
Net surplus for the year	355,103	35,634
Add non-cash items:		
Depreciation and amortisation	3,213	2,771
	3,213	**2,771**
Add (less) movements in other working capital items:		
Premiums receivable	(930)	133
Other receivables	(189)	671
Prepaid reinsurance	(320)	(299)
Interest accrued	15,355	7,556
Provision for employee entitlements	(6)	(3)
Trade payables	(167)	(423)
Outstanding claims	2,944	(10,215)
Unearned premium	853	289
Unexpired risk liability	6,000	–
	23,540	**(2,291)**
Add (less) items classified as investing activity:		
Discount income and investment price revaluations	(124,977)	208,391
Loss on disposal of property, plant and equipment	10	27
	(124,967)	**208,418**
NET CASH INFLOW FROM OPERATING ACTIVITIES (GST EXCLUSIVE)	**256,889**	**244,532**

21 CREDIT RATING

The Commission has been assigned an insurer financial strength rating of AAA (extremely strong) as accorded by international rating agency Standard & Poor's on 25 September 2009.

22 EVENTS AFTER THE STATEMENT OF FINANCIAL POSITION DATE

Subsequent to the balance date, on 4 September 2010 a magnitude 7.1 earthquake, centred near Darfield, Canterbury, caused severe damage across the region. At this stage the net cost to the Commission is expected to be in region of $1 to $2 billion. This will be funded through existing cash resources, the liquidation of some investments and reinsurance. The Commission's re-insurance scheme provides cover of $2.5 billion with an excess of $1.5 billion.

Statement of service performance

FOR THE YEAR ENDED 30 JUNE 2010

Output Class 1: Claims' handling

This output class comprises the maintenance of EQC's state of readiness to meet the requirements of the Crown for the compensation of residential property owners following a natural disaster and the incorporation of this readiness, so far as is possible, into normal daily operations.

It contributes to the impact of *enhanced community recovery through delivery of Act entitlements to claimants in the fastest practicable time by means of the Catastrophe Response Programme* and through that to the Government's outcome of *safer communities and rapid recovery from natural disasters.*

Performance targets and results

1. The programme's plans and schedules to maintain its effectiveness are adhered to (e.g. schedules for document maintenance, testing and training).

   Achieved. *Plans and schedules adhered to and all training and exercises undertaken.*

2. Keeping settlement time within the following limits:

   a. For claims under the imminent loss provisions, 90% of claimants receive their entitlements within one year of the date of loss.

      Not Achieved. *There were 422 imminent loss claims settled during the year. 322 (76%) were settled within the 12-month period targeted. Of the 100 that were not settled in the 12 month period 40% were over $200,000 and required significant engineering advice.*

   b. For other claims, when there are fewer than 10,000 claims open in total, 80% of claimants receive their entitlements within 90 days of the date of loss.

      Achieved. *90% of other claims were settled within 90 days of lodging their claim.*

3. EQC has responded to its risks and challenges as described in the following table.

EQC'S CHALLENGES AND RISKS	EQC'S RESPONSE	RESULTS
An ability to assess rapidly the requirements of an EQC response to a natural disaster occurrence.	Development of computer applications that provide the analysis and insights to enable the necessary assessments and decisions to be made (EQC has an earthquake hazard and analysis model, a systems dynamics model and a web-based claims management system).	**Achieved.** *Computer applications maintained and enhanced. Models used as basis for calculating event response.*
Limited numbers of loss adjusters, engineers, valuers and other specialists required to process claims.	Secure agreements with loss adjusting firms and other service providers, in Australia and New Zealand, for the provision of specified numbers of people in a disaster.	**Achieved.** *Agreements are in place with New Zealand and Australian loss adjusting firms for the provision of specified numbers of people in a disaster.*
	Support for New Zealand loss adjusting firms to recruit and train new entrants to the industry.	**Achieved.** *The 'new entrant' scheme was established and the first three loss adjusters were engaged.*
	Retain a cadre of loss adjusters on a guaranteed minimum income.	**Achieved.** *22 loss adjusters and estimators contracted.*
EQC's ability to estimate the amount needed to meet claims could be hampered by the effect on construction costs of post-event demand surge.	Fund research into the likelihood and extent of post-event demand surge and its possible effect on EQC's claims costs.	**Achieved.** *A study of post-event demand surge is almost complete. Final report is due in August 2010.*

Output Class 2: Research

This output class includes research in fields relevant to natural disaster damage, methods of reducing or preventing natural disaster damage, and the insurance provided under the Earthquake Commission Act.

Through its advocacy of, and investment in, science and engineering research, EQC contributes to natural hazard assessment and disaster prevention in New Zealand. The Commission's research activities contribute to the outcome of *safer communities and rapid recovery from natural disasters* with the impact of *reduction in the Crowns liabilities arising from natural hazard events and improvement in the resilience of communities to natural hazards*. Research into construction and engineering methods can also have economic spin-offs and contribute to a knowledge-driven economy.

Performance targets and results

1. A 2009–10 competitive funding round that meets the budget and timetable approved by the Board.

   Achieved. *19 projects were approved for funding for a total of $800,000 over two years.*

2. Previous round projects are proceeding or being completed on time, within budget and are meeting their objectives.

   Achieved. *17 projects were completed in the year 1 July 2009 to 30 June 2010. Two projects are behind time but remain within budget and are meeting intended objectives.*

3. All other projects are proceeding or being completed on time, within budget and are meeting their objectives.

   Partially achieved. *Seven university postgraduate student research projects were completed in the year to 30 June 2010. 21 projects are in progress, 13 are within budget and meeting objectives and the other seven have just commenced. Two university projects were terminated during the year because the students' enrolments were terminated by the respective universities.*

4. All partners in the Science to Practice programme are meeting the conditions under which EQC support is provided.

   Achieved. *One Science to Practice project was completed in the year to 30 June 2010. Three projects are in progress, and meeting the conditions under which support is provided.*

5. Standards New Zealand projects receiving EQC funding are proceeding and being completed on time, within budget and are likely to meet, or have met, their objectives.

   Not applicable. *No projects funded in the 2009–10 year.*

6. The capability building programmes are meeting contracted requirements for teaching, research and public activities.

   Achieved. *EQC's university-based teaching and scholarship programmes have contractual arrangements specifying EQC's requirements and these have been fulfilled.*

7. GeoNet is meeting contracted requirements for maintenance, development and timely provision of data and hazard warning information.

   Achieved. *All service level requirements for GeoNet were fulfilled on time and within budget.*

8. EQC has responded to its risks and challenges as described in the following table.

EQC'S CHALLENGES AND RISKS	EQC'S RESPONSE	RESULTS
The significant variability in land-use planning and practice throughout New Zealand (a strategic review of GeoNet in 2004 identified this issue).	Support for both a Standards New Zealand Hazard Management Standard and the identification of practical ways to improve planning for the management and use of landslip-vulnerable land.	**Partially Achieved.** *A cross-disciplinary study "Slope Stability and Land Use: Improving Planning Practice," was published in September 2009.*
Transforming research outputs to social outcomes.	A Science to Practice programme fosters the transfer and uptake of science research by end users.	**Achieved.** *Three cross-disciplinary initiatives were advanced comprising:* (i) *a study of slope stability and landuse planning to improve planning practice;* (ii) *a study of the impact of volcanic ash on New Zealand roofing materials; and* (iii) *assisting territorial authorities with the statutory review of earthquake-prone building policies.*
Sustenance of national capacity for timely and high quality science research for risk assessment and mitigation.	Contract with GNS Science for the support of the national hazard monitoring system GeoNet. Funding of the following programmes: + the Leicester Steven Lectureship in Engineering at the University of Canterbury; + the Institute of Earth Science and Engineering at the University of Auckland; + the EQC Fellowship in Natural Hazards Planning at Massey University; and + the EQC Fellowship in Seismic Studies at Victoria University.	**Achieved.** *During the year, EQC renewed its capability funding agreements for research and teaching programmes at Canterbury, Victoria and Massey universities, for a further five years. Also renewed was an agreement with GNS Science for the operation and maintenance of GeoNet over the next decade.* *Under contracts with GNS Science, EQC continues its support as lead stakeholder of the projects: "It's Our Fault" (Wellington Seismic Risk Programme), and "DEVORA" (Determining the Volcanic Risk in Auckland). EQC is committed to matching the funding of other stakeholders and this financial year both programmes have gained support of an extra stakeholder each.*
Enabling the intensive research opportunity presented by disasters at home and overseas.	Internal decision and funding systems are sufficiently robust and flexible to respond to urgent needs.	**Achieved.** *EQC contributed (along with other agencies) to successful fact-finding missions following earthquakes in Indonesia and Chile, with practical lessons learned for application to New Zealand.*

Output Class 3: Public education

This output class has two elements:

- public education about seismic hazards and methods of reducing or preventing damage;
- public education about EQC's role and the importance of home insurance.

These outputs reflect EQC's functions under Section 5(1)(e) of the Earthquake Commission Act: "Facilitate research and education about matters relevant to natural disaster damage, methods of reducing or preventing natural disaster damage, and the insurance provided under this Act." They contribute to the impact of *Improved levels of knowledge and activity of New Zealanders to make their homes safer from natural perils, understand EQC's role and take out adequate insurance.*

In turn, this impact contributes directly to the Government's outcome of *safer communities rapid recovery from natural disasters* and indirectly to the outcome of *efficient management of the Crown's assets and liabilities,* because the Crown's fiscal risk is reduced as more households take precautions against damage from seismic events.

Performance targets and results

1 Sponsorship for museums and other exhibitions that meet set targets including visitor numbers and brochure distribution.

Achieved. *The new EQC kiosk at Te Papa opened in March. The Board agreed terms for a new sponsorship arrangement with the Auckland Museum in April and a new three-year sponsorship agreement with the Volcanic Activity Centre was completed. Visitor numbers and brochure distribution for all museums were at acceptable levels (targets defined broadly, i.e. numbers consistent with or greater than previous years).*

2 One regionally-based campaign with local partners.

Achieved. *The Kapiti pilot programme was carried out in August. This involved setting up a quake safe experiential house, running a district-wide quake safe competition, carrying out door-to-door mitigation surveys and providing assessments at no cost to homeowners. These activities were supported by intensive community-based advertising, sponsorship, a website and public relations activities. Partners included the local Civil Defence operation, Kapiti Lions, Paekakariki playcentre parents, local radio stations, newspapers and several local businesses.*

3 Production of one virtual field trip for school students.

Achieved. *A virtual field trip to the Wellington Fault was undertaken during May. Class enrolments (122) for the trip were well ahead of expectations, reflecting the popularity of the topic.*

4 The number of New Zealanders or householders in regions that EQC has targeted exceeds the national figures established by on-line survey at 1 October 2008, by 10 percentage points by the end of each regional campaign.

	1 OCT 2008	TARGET	FOLLOWING KAPITI PUBLIC EDUCATION CAMPAIGN
Level of knowledge about making homes safer	52%	62%	52%
Taken steps to make homes safer	52%	62%	95%
Understand EQC role	72%	82%	69%

Partially achieved. *One target was met – steps taken to make homes safer. Two of the targets were not met – levels of knowledge about making homes safer and understanding EQC's role. It was decided that the component parts of the Kapiti programme should be used to develop a community-based public education tool-kit, available to groups, organisations and local authorities throughout the country. This approach offers a better means of fostering community programmes in New Zealand than a separate EQC-led campaign.*

5 The number of insured households at 30 June 2012 exceeds (on a national basis) the figures established by on-line survey at 1 July 2008 by three percentage points. These figures were 90% for dwellings and 88% for contents.

In progress. *End of reporting period not yet reached. The April 2010 survey results show insurance for dwellings at 97% and insurance for contents at 87%.*

6 EQC has responded to its risks and challenges as described in the following table.

EQC'S CHALLENGES AND RISKS	EQC'S RESPONSE	RESULTS
Experience in New Zealand and overseas is that public expectations, including expectations of EQC are developing rapidly.	Cognisance of public expectations and attempts to influence them where appropriate.	**Achieved.** *Targeted advertising to public of claims deadlines in a range of media following significant natural disaster events.*
Communications methods and habits are changing rapidly.	Use of modern ways of communicating, including use of new media and innovative use of old media such as exhibitions at Te Papa and Auckland Museum.	**Achieved.** *EQC employed a range of methods with which to communicate its messages, including the internet, press advertising, newsletters, museum exhibitions and a regional public education programme.*
The public tends to downplay the risk of disasters affecting them and fails to take proper action to prepare.	Due consideration of the research that has been done into achieving behavioural change in society.	**Achieved.** *Regional public education programme undertaken in Kapiti. This move reflected research that indicates EQC must engage more actively and closely with communities to achieve its goals.*
The public is swamped with advertising and social marketing messages and EQC's message may not attract attention.	Identification of 'trigger points' at which EQC's mitigations message will be particularly apposite to New Zealand families. A regional focus to make EQC's message more direct and immediate in the area targeted.	**Achieved.** *Purchase of a house identified as a trigger point. Research on the vulnerability of house foundations to earthquake damage carried out.* *Kapiti regional public education programme undertaken during September.*
The opportunity for grabbing the public's attention provided by the news of a disaster occurrence at home or overseas should be recognised and prepared for.	EQC's decision and funding systems will remain sufficiently robust and flexible to respond to urgent needs.	**Achieved.** *Mitigation advertising carried out following the Samoan tsunami, the Solomon Islands earthquake and the Chile earthquake. New internet advertisements set up for automatic display following natural disaster events.*

Output Class 4: Policy advice

This output class includes the provision of policy advice to the Government on issues related to EQC's statutory functions, including:

- natural disaster damage;
- methods of reducing or preventing natural disaster damage;
- Government response to disasters;
- relevant risk management issues;
- management of the Natural Disaster Fund and protection of its value; and
- terms and conditions of the insurance.

It contributes to all of EQC's impacts, and through them to the Government's outcomes of *safer communities and rapid recovery from natural disasters* and *efficient management of the Crown's assets and liabilities.*

Performance target and result

1 All requests for participation in policy preparation are met to the satisfaction of the Minister or departments concerned and are within agreed timelines.

Achieved. *All Ministerial enquiries during the year were responded to within agreed timelines.*

Output Class 5: Administration of the Act Insurance Scheme and Natural Disaster Fund.

This output class seeks to optimise the Commission's contribution to community recovery from disaster by development and maintenance of the financial capacity to meet all obligations imposed by the Act. This involves administration of the Fund, including collection of the premiums payable and, so far as reasonably practicable, protection of the Fund's value through the investment of money held in the Fund and reinsurance in respect of the whole or part of the insurance provided under the Act. It reflects EQC's functions as set out in section 5(1)(b), (c) and (d) of the Act and contributes directly to the Government's outcome of *efficient management of the Crown's assets and liabilities.*

Performance targets and results

1 Negotiation of a reinsurance programme that reduces the net risk to the Natural Disaster Fund and the Crown.

Achieved. *Computer modelling shows the reinsurance programme for the 2009–10 year reduces the risk of the Fund falling to zero in any year by 56% and of falling below $2 billion in any one year by 52%, compared to having no insurance in place.*

2 Investment performance that achieves the targets set in the *Statement of Investment Policies, Standards and Procedures* set out below.

ASSET CLASS	RESULTS	BENCHMARK/ TARGET RETURN
NZ Government stock	7.9%	8.2%
NZ Government inflation-indexed bonds	9.9%	9.9%
Bank bills (registered certificates of deposit) / Treasury bills	2.7%	2.5%
Passive global equities	4.1%	3.8%
Active global equities	4.5%	3.8%
Total Portfolio*	**6.8%**	**6.8%**

* The target return for the total portfolio is 1% plus the New Zealand Government stock index return, over a rolling 10-year period. The structure has not been in place long enough to compare 10-year returns. For the five years to 30 June 2010, the actual portfolio return was 5.2% versus the target of 7.8%.

3 EQC has complied with its asset allocation strategy and investment managers have complied with their agreements.

Achieved. *This included investing in approved asset classes only, maintaining asset classes within specified ranges, ensuring cash was invested in banks with high credit ratings, receiving compliance and audit reports from custodians and fund managers, and reporting on the Fund to the Board and Investment Committee.*

4 EQC's investment management costs are in line with international peers.

Achieved. *An international investment benchmarking company employed by EQC shows that EQC's investment management costs are below the median of its international peers.*

5 EQC has managed and administered the Fund in a manner consistent with best practice portfolio management, maximising return without undue risk to the Fund as a whole.

Achieved. *Best practice portfolio management was maintained and the Fund realised a positive return for the year.*

6 EQC has acted in accordance with its responsible investment policy standards and procedures. It includes in its annual report comment on the extent to which social, ethical and environmental issues have been considered in EQC's investment process and EQC's proxy voting policy.

Achieved. *EQC has met its responsible investment obligations and the annual report meets these requirements.*

7 EQC has validated the premiums paid to it by insurance companies and investigated and resolved discrepancies or qualified audits.

Achieved. *The programmes of records checking and external audit were completed. Seven external audit opinions were received and none were qualified.*

8 EQC has responded to its risks and challenges as described in the following table.

EQC'S CHALLENGES AND RISKS	EQC'S RESPONSE	RESULTS
Investment of the Fund to protect its value and maintain standards of international best practice (including with regard to responsible investing), is a complex task requiring specialised knowledge, wide-ranging expertise and constant vigilance.	Employ the necessary expertise on employees to be able to manage and control, with assistance from professional advisers, the custodians, investment managers and other specialists who can ensure required standards are achieved and maintained.	**Achieved.** *EQC investment team has a full complement of employees with the necessary expertise to carry out its functions.*
Building costs may continue to increase, resulting in higher payouts for EQC, and increased risk to the Fund. The maximum sums insured under the Act have not been adjusted since the Act's inception in 1993, compromising their original purpose.	Making the case for the maximum sums insured (the "caps") on EQC's cover to be adjusted to account for these inflationary trends and stabilise EQC's liability.	**Achieved.** *This process was concluded in the previous financial year, and no further action was required during the current financial year.*
Reinsurance costs and the financial security of EQC's reinsurers are influenced by external factors like major disasters overseas and the performance of the financial markets.	Manage potential volatility of reinsurance pricing by forward purchasing and, if competitive, alternative risk transfer products.	**Achieved.** *The 2010/11 reinsurance programme continues the three-year tranche arrangement used to manage the volatility of the reinsurance premium levels. No alternative risk transfer products have yet been found to be as effective as current arrangements at achieving EQC's objectives for its reinsurance programme.*
	Manage counterparty credit risk by applying a minimum claims paying ability rating of A (Standard and Poor's) over the entire programme, limiting capacity provided by companies rated A-, market surveillance and analysis by EQC's reinsurance brokers, and maintaining the ability under the reinsurance agreements to replace reinsurers on downgrading.	**Achieved.** *The weighted counterparty risk rating of the reinsurance programme was A+. At the time of the last review (March 2010) the capacity of companies rated A- was 4.5%. It is now within EQC's target of a maximum of 5%. The treaties retain the clause that allows cancellation by EQC of reinsurers that are downgraded.*

Output Expenditure for the Year Ended 30 June 2010

OUTPUT CLASS	ACTUAL REVENUE	ACTUAL EXPENDITURE	BUDGET REVENUE	BUDGET EXPENDITURE
Claims handling and the Catastrophe Response Programme*	Nil	$7.4 million	Nil	$8.6 million
Research	Nil	$10.8 million	Nil	$11.1 million
Public education	Nil	$2.4 million	Nil	$3.1 million
Policy advice	Nil	Nil	Nil	Nil
Management of the Natural Disaster Fund	$471.5 million	$57.6 million	$414.2 million	$62.7 million

* This includes only the costs of operating the Catastrophe Response Programme and excludes claim settlements and directly associated costs.

Other disclosures

Good Employer Compliance

EQC has met all the requirements of its equal employment opportunity policy.

The Commission takes its role as a good employer of 22 employees seriously because human resources are integral to its business. To ensure employees regard EQC as a good employer, the Commission will continue to:

- Demonstrate leadership and vision that articulates EQC's values and the importance of its employees;
- Provide equal employment opportunities for employees (see below);
- Provide opportunities for employee participation in organisational decisions;
- Encourage employees to develop to meet their aims and aspirations through internal and external training, coaching and mentoring;
- Implement an impartial, transparent employment process and equal opportunities to move up, through and out of the organisation in a positive way;
- Provide a comprehensive introduction to the organisation setting out EQC's values and objectives;
- Take account of the need for employees to balance work with the rest of their lives;
- Utilise performance management practices that are transparent and fair;
- Have a transparent, fair, gender neutral remuneration system;
- Provide a working environment that is free from all forms of harassment and bullying and provide safe and fair means of dealing with complaints;
- Provide a healthy and safe workplace, observing occupational safety and health requirements at the corporate office and as part of the Catastrophe Response Programme, to ensure temporary field offices and claims sites are safe for the Commission's workers.

As an Equal Employment Opportunities (EEO) employer, EQC is committed to the principle of fair and equal treatment for all its employees.

This means that all its decisions about its employees must be free of unfair discrimination based on colour, race, ethnic or national origin, sex, marital status, religious or ethical belief or disability.

EQC will ensure that it does not discriminate on these grounds in deciding what terms or conditions of work, or fringe benefits, or opportunities for training, promotion or transfer it offers to its employees.

EQC will work towards the removal of any barriers it may have to the employment or advancement of suitably qualified disabled people, should the opportunity arise to take such people onto its staff.

EQC recognises the importance of volunteers contributing to social development, the environment and the economy, and supports employees participating in voluntary community work from time-to-time, while ensuring that professional obligations are met.

EQC has a confidential Employee Assistance Programme, under which any employee may seek assistance from a contracted external service provider if non-work issues are affecting work performance.

		2009/10	2008/09	2007/08
Average length of service		8 years	8.2 years	7.2 years
Employee turnover		4	–	5
Total employees at 30 June		21*	22	21*
Gender	Male	11	12	11
	Female	10	10	10

*One vacancy existed at 30 June 2010 and 2008.

Investment Processes – Environmental, Social and Governance Considerations

Principles

The Commission considers that responsible investment decision-making that takes account of environmental, social and governance (ESG) considerations is part of evolving best practice. Responsible investment actions can include engagement, voting, exclusion of certain investments, and/or divestment.

The Commission, at its discretion, and provided that it is consistent with its obligation to invest the Fund on a prudent, commercial basis, may consider other issues arising from the Fund's investments. In doing so, the Commission may take into account factors such as whether the issue is contrary to New Zealand law and New Zealand's international agreements, or is inconsistent with Crown actions.

The Commission is a signatory to the United Nations Principles for Responsible Investment (UNPRI), and acknowledges internationally agreed standards for responsible corporate behaviour and investment. As such, the Commission aims to encourage companies in which it invests to meet internationally agreed standards for responsible corporate behaviour.

Implementation

If companies invested in are found to have corporate practices that breach its responsible investment policy, the Commission will consider engaging with the company either directly or in conjunction with other investors, or taking other shareholder action. The Commission believes that it can, in most instances, have a greater impact on company practices through dialogue with company management in conjunction with others, than through immediate divestment.

As a last resort the Commission may divest of investment in companies that are found to have corporate practices that breach its responsible investment policy.

Investment Managers

The Commission appoints external investment managers to manage portions of the Fund. As part of the selection process the Commission assesses the overall investment management capabilities of candidate managers, including the ability to implement the Commission's requirement to avoid prejudice to New Zealand's reputation as a responsible member of the world community.

Investment managers are required to be vigilant against the effects on companies' long-term performance prospects that could arise from any practices which alienate civilized society including socially and environmentally irresponsible behaviour.

Maintaining open dialogue with investment managers, including in relation to the requirement to avoid prejudice to New Zealand's reputation, is considered to be critical to the achievement of the Commission's objectives.

In addition, consistent with the UNPRI, the Commission encourages its investment managers to integrate ESG factors into evolving research and analysis and to undertake and report on ESG-related engagement. The investment managers report to the Commission on their application of the responsible investment requirements, on a six-monthly basis.

Investment managers are formally instructed of any exclusion or divestment decisions by the Commission.

Exclusions

In line with the obligations and responsibilities of the responsible investment policy, the Commission and its investment managers do not invest the Fund in the following:

- Organisations engaged in the development, production, transfer, possession, acquisition, stockpiling or use of anti-personnel mines, or
- Organisations engaged in the production of cluster munitions, or
- Organisations engaged in the manufacture, simulated testing and/or refurbishment of nuclear explosive devices, or
- Manufacturers of cigarettes and tobacco.

Future Responsible Investment Development

EQC's approach to responsible investment is evolving and the Commission will continue to work with the other New Zealand Crown financial institutions (CFIs) to improve its ability to meet its responsible investment obligations.

All CFIs are required to avoid prejudice to New Zealand's reputation as a responsible member of the world community. CFIs, including EQC, are sharing responsible investment research resources. The responsible investment unit of the New Zealand Superannuation fund undertakes significant background work and secretarial services and all CFIs now have access to the output of a leading global research company in responsible investment. The Commission's arrangements with the New Zealand Superannuation Fund and our membership of the United Nations Principles Responsible Investment give us mechanisms to engage with investee companies which are believed to be at risk of non-compliance with globally expected standards.

Proxy Voting Policy

The Commission believes that good corporate governance should maintain a balance between the rights of shareholders on one hand and the needs of the corporate board and management to direct and manage the company's affairs on the other.

Responsible governance should reinforce a culture of integrity and transparency, contribute to the achievement of strategic goals, ensure Board alignment with shareholder interests, reinforce and maintain good business ethics, and recognise environmental and social considerations.

The Commission believes that good corporate governance will also maximise returns to the Fund without undue risk.

Voting rights are important to the Fund for maintaining shareholder oversight of directors and company policies. The Commission will use its voting rights to encourage good corporate governance.

Voting Rights

Pooled Accounts

The Board will retain the right to exercise any vote attached to units held in a pooled account. The right to exercise any vote attached to a share or unit within a pooled account will normally rest with the manager of the account.

Directly held Accounts

Any voting rights attached to any securities that form part of the portfolio shall be exercised by the manager:

- As directed by EQC by written notice to the manager; or
- If no such direction is made, in accordance with the manager's duties and obligations under their agreement and in particular, avoiding prejudice to New Zealand's reputation as a responsible member of the world community.

Statement of Responsiblity

THE BOARD IS RESPONSIBLE FOR THE PREPARATION OF THE EARTHQUAKE COMMISSION'S FINANCIAL STATEMENTS AND STATEMENT OF SERVICE PERFORMANCE, AND FOR THE JUDGEMENTS MADE IN THEM.

- The Board and management are responsible for establishing and maintaining a system of internal control designed to provide reasonable assurances as to the integrity and reliability of the financial reporting.
- In the opinion of the Board and management, the annual financial statements for the financial year fairly reflect the financial position and operations of the Commission.

Signed on behalf of the Board:

Chairman

30 September 2010

Commissioner

30 September 2010

Directory

MINISTER IN CHARGE OF THE EARTHQUAKE COMMISSION

THE HON BILL ENGLISH

COMMISSIONERS

M C WINTRINGHAM CNZM, BA (HONS)
CHAIRMAN

K B TAYLOR BCA, BSC, FIA(LONDON), FIAA, AFIOD
DEPUTY CHAIRMAN

D K BOVAIRD BCOM, FCA

R J HOOPER BE (HONS), PHD, FIPENZ
(RETIRED FROM THE BOARD DURING THE YEAR)

G A MCLACHLAN LLB

G T MURIWAI MCOM (HONS), CA
(RETIRED FROM THE BOARD DURING THE YEAR)

L M ROBERTSON BCOM, DIP BANKING, FINFINZ, GAICD, AINSTD

SENIOR MANAGEMENT

I SIMPSON BSC (HONS), MBA
CHIEF EXECUTIVE

P R JACQUES BSC, DIPMGT, DIPACC, CA, CFIP
CHIEF FINANCIAL OFFICER

L R DIXON GRADDIPBUSSTUDS (INS MGT), ANZIIF (FELLOW)
INSURANCE MANAGER

H A COWAN PHD
RESEARCH MANAGER

AUDITOR

DELOITTE, WELLINGTON
(ON BEHALF OF THE AUDITOR-GENERAL)

BANKER

NATIONAL BANK OF NEW ZEALAND, WELLINGTON

SOLICITORS

CHAPMAN TRIPP, WELLINGTON
DLA PHILLIPS FOX, WELLINGTON

INVESTMENT ADVISOR

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- Landslip above Kawakawa Bay
- Diver installing tsunami equipment at Lottin Point, East Cape

EQC Team

Giselle McLachlan
Commissioner

Linda Robertson
Commissioner

Denise Bovaird
Commissioner

Keith Taylor
Commissioner

Sophie Gordon
CRP Support Officer

Kate Liddle
Case Manager

Hugh Cowan
Research Manager

Lance Dixon
Insurance Manager

Michael Daly
Manager Investment Strategy

Lisa Davidson
Accounts Officer

Kaya Yamabe & Donna Cleland
Receptionists

Joanne Clough
Finance Manager

Valerie Michael
Investment Analyst

Tony Sheehan
Training Manager

Evelina Fa´amausili
Senior Accounts Officer

Graham Booth
Claims Manager

Doug Bent
Operations Manager

Rochelle Milne
Assistant Claims Manager

Colin Klenner
IT Manager

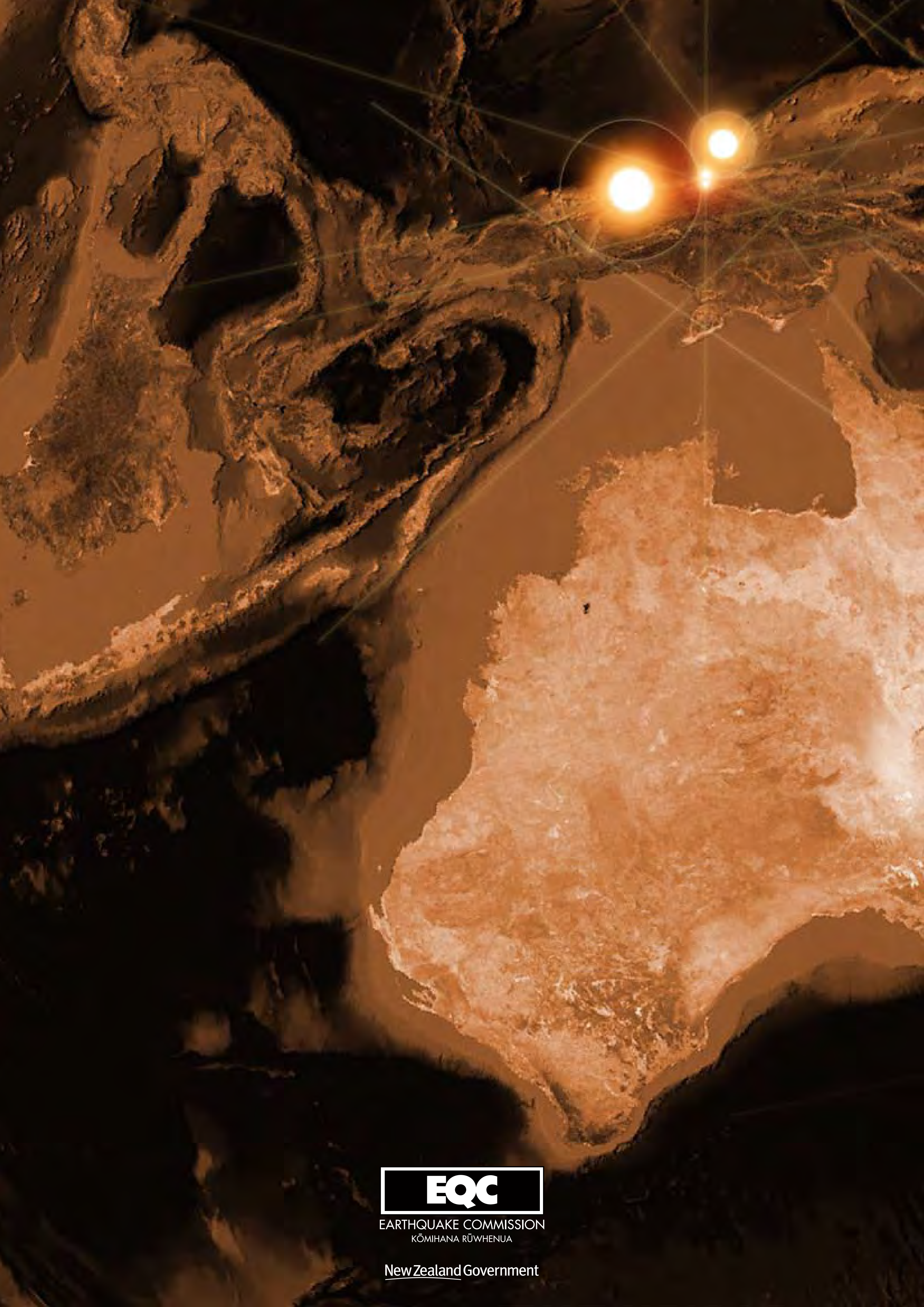
Priscilla Cheung
Executive Secretary

Joanna Martin
Communications Adviser

Phillip Jacques
Chief Financial Officer

Derek Gibb
Compliance Manager

Tony Burton
Network Administrator



EQC

EARTHQUAKE COMMISSION

KŌMIHANA RŪWHENUA

New Zealand Government