NIBA
National Insurance Brokers Association.

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NSW Independent Flood Inquiry,
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NIBA Submission: NSW Independent Flood Inquiry

About NIBA

NIBA is the peak representative body for the intermediated general insurance industry. NIBA represents approximately 450 member firms and 15,000 individual brokers including large, multinational insurance brokers, Australian broker networks, and small to medium-sized businesses located in cities, and regional areas right around Australia.

NIBA aims to promote the role of insurance brokers and the role they play in supporting and advising their clients on risk and insurance matters. NIBA provides this knowledge and expertise to governments and government agencies to promote understanding of the operation of general insurance markets.

Unlike an insurance agent, who works exclusively for one or more general insurance companies, general insurance brokers are professional risk advisors who work on behalf of their clients to protect their assets and businesses.
Insurance brokers work with their clients to:

- understand, assess and manage their risks
- develop appropriate risk-transfer and risk financing strategies;
- seek cover from insurance markets that meet the above needs and strategies in a cost-effective manner;
- act as the client's advocate during a claim; and
- assist with renewing insurance and recommend changes.

In performing these duties, insurance brokers act as agents of their clients and have statutory, common law and professional obligations to act in the best interests of their clients. At times, brokers may act on behalf of an insurer when providing certain services. When this occurs, brokers have a duty to communicate this to their clients.

Insurance brokers represent the interests of the purchasers of insurance, the policy-holders, and not those of insurance companies. Consequently, comments made by NIBA, and its members are made on behalf of its members and the public that purchases insurance not on behalf of insurance companies.

Introduction

NIBA welcomes the opportunity to provide these comments to the NSW Floods inquiry. The damage caused by the recent floods in Northern NSW have demonstrated the need for a new approach to natural disaster mitigation, response, and recovery.

On average, natural disasters cost the Australian economy $18.2 billion every year, with that amount predicted to increase to $39 billion by 2050. Flooding is Australia's costliest natural hazard-related cause of disaster when both tangible and intangible

losses are taken into consideration. To date, 180,245 claims have been lodged for damage arising from flooding in south-east Queensland and New South Wales with the cost of claims estimated to be $2.523 billion.

NIBA and its members are committed to helping their clients and the broader public through this difficult process, having established a claims support initiative, whereby qualified, professional brokers offer their skills and expertise to advise and assist policyholders with their insurance claims.

Looking beyond the immediate recovery phase, NIBA has a number of concerns regarding the affordability of insurance, land-use planning, and the need for significant investment in public and private flood mitigation works.

Insurance affordability and emergency services funding

Ensuring the states' emergency services are adequately funded is vital to governments' ability to respond to natural disasters. Unlike most state and territory governments which fund their emergency services through property-based levies, services in NSW are funded through an insurance-based levy, the Emergency Services Levy (ESL) which is levied on all general insurers in Australia, based on their market share.

This charge is then passed on to the policyholders in the form of an ESL component on general insurance policies as a percentage of the base premium. Policies that attract ESL include; residential building and/or contents insurance, commercial property insurance, motor vehicle insurance, marine and baggage insurance, and some forms of crop and livestock insurance. General insurance contributions account for almost 75 per cent of emergency services funding, with local councils and the state government contributing the remainder. The general insurer contribution for the 2020-21 financial year has been set at $1,089,966,770 up from $898,000,000 the previous year.

State	Emergency services funding model
Australian Capital Territory	Property-based funding model - Residential and rural properties pay $91.20 - Commercial properties levied on the basis of the average unimproved land value over three years
New South Wales	Statutory contributions model - Insurers contribute 73.7% - Local government contributes 11.7% - State government contributes 14.6%.
Victoria	Property-based funding model - Levy is a fixed fee plus a variable component derived from capital value improved, location and classification. - Fixed charge varies for residential and commercial properties.
Queensland	Property-based funding model - Urban Fire Levy contributes 73% of funding with State government and user charges making up the remainder. - Amount of levy is dependent on the "class" of the urban district (i.e., where the property is situated); the activity carried out on the property or the use to which the land is used and the size and nature of any improvements on the land.
Western Australia	Property-based funding model - Levy applied on the gross rental value of all immobile properties. - No levy imposed on motor vehicles. - State is divided into fire levy categories according to level of service (i.e., extent of emergency service provision and access). - Minimum charge of $43 with maximum levy payable by households of $225 and commercial property owners $130,000
South Australia	Property-based system funding model - Emergency Service Levy levied on capital values for fixed property and also on motor vehicles and other mobile capital. - Levy on fixed property is a fixed fee ($50) plus a variable component derived from capital value, an "area factor", land use "factor" and the levy rate. - A fixed fee applies for motor vehicles.
Tasmania	Statutory contributions model. - Levy on insurance policyholders of 28% of gross premium for all commercial insurances against fire. For marine and cargo insurance levy is 2% of gross premium and 14% for aviation - Local government levies assessed on annual value of properties with minimum charges applicable. - A fixed fee of $14 applies for motor vehicles
Northern Territory	Funded through consolidated revenue

Unlike property-based funding models which spread the burden of funding emergency services across the broadest range of beneficiaries, insurance-based levies have been widely criticised for being inequitable, forcing responsible property owners to pay for a service that is beneficial to all of society, whilst those who do not insure their risks continue to receive the benefits.

According to standard taxation principles, a well-designed tax system is characterized by efficiency, equity, simplicity, and transparency. A number of public inquiries, including the HIH Royal Commission, have been critical of insurance taxes because they perform poorly against these basic principles. The 2008 New South Wales IPART Review concluded that emergency services funding was amongst the least inefficient state taxes. While the Victorian Royal Commission into the Black Saturday bushfires found that a similar insurance-based levy was "inequitable" as it forces responsible property owners - those who have adequately insured their properties against loss- to shoulder the costs of funding the emergency services rather than a fairer system in which all property owners collectively fund state emergency services.

The ESL has also been criticised for being a needlessly opaque and complex funding model. The ESL is generally poorly understood by the public, with individual policyholders often unaware of the extent to which they are funding New South Wales emergency services. Furthermore, due to the unpredictable nature of the insurance market, the amount collected by insurance companies as the ESL may not equate to actual statutory contributions made. Dr Ken Henry, the Chair of the Commonwealth's Review of Australia's Future Tax System (AFTS) and head of the Commonwealth Treasury, referred to insurance taxes as "bad taxes" and said that a tax on a broader base would be more efficient, equitable and transparent.

The effect of these taxes is compounded by both GST and stamp duty, which are both levied on top of the base premium and ESL contribution. This compounding of taxes results in a significant increase in premiums that can have serious consequences for policyholders who may already be struggling with insurance affordability. In NSW taxes and levies can increase the cost of some insurance policies by up to 70 per cent. Recognising the impact these taxes have on insurance affordability and risk mitigation, the ACT abolished stamp duty on all insurance premiums, meaning policyholders only pay a single transaction tax (GST) on their insurance premiums. For policyholders, especially those impacted by the turbulent events of the last few years, these taxes make insurance an unaffordable luxury, rather than a necessity of home ownership. Policy holders may be forced to reduce the sum insured value of their property, forgo important additional cover, such as flood cover or go without insurance entirely, leaving them open to significant financial liability if a disaster were to occur. The recent floods in Northern NSW

highlighted multiple instances where owners lost their properties and had not elected to take out flood cover on their respective properties. Some of these were organisations who had been supporting their community for more than 30 years.

Under and non-insurance

Under-insurance is generally regarded as occurring when the sum insured is insufficient to enable full replacement of the damaged or destroyed property or the re-establishment of the business where a commercial enterprise is involved. This amount can differ significantly from the market value of the property, which is also commonly used in insurance. Often under-insurance only becomes apparent following a large-scale insurable event, such as the recent floods. Because of this it is extremely difficult to estimate the rate of under-insurance nationwide. Similarly, it is not always easy to establish the replacement value of a property or business at the time a policy is taken out; as the replacement value of a property can vary based on inflation, new building standards, or circumstances arising at the time of the claim.

An Insurance Council of Australia (ICA) report into non-insurance found that states with higher rates of insurance-based taxes also have higher rates of non-insurance for both building and contents insurance. Similarly, the ACCC Northern Australia Insurance Inquiry found that a leading contributor to a property owners' decision to underinsure or not insure their property was affordability. Modelling by the ICA shows that the increase in premiums as a result of ESL increases will result in a $20 million reduction in pre-tax expenditure on insurance.

The artificial inflation of premiums caused by these taxes acts as incentive for property owners to arrange alternative risk-financing mechanisms, such as mutual pools and captive insurance, which do not attract the levy. This means that when a policyholder leaves the traditional insurance model, the remaining policyholders must shoulder a higher proportion of the ESL.

All other mainland States have abandoned insurance-based levies in favour of a fairer, more broad-based property levy, whereby those who receive the benefits of the emergency services (property owners) contribute to their funding via council rates. Such an arrangement would overcome the major deficiencies of the current insurance-based models, identified within this submission.

There are a number of property-based funding models from which the New South Wales government could borrow in developing their own, with Victoria, Queensland, Western Australia, South Australia, and the ACT each providing examples for New South Wales to follow. NIBA strongly supports a move to funding emergency services by way of a property levy. Such a move would increase efficiency, effectiveness, simplicity, and transparency. It would eliminate the current compounding of state and federal taxes and encourage individuals and businesses to appropriately mitigate their risks, reducing reliance on government assistance post disaster.

Mitigation

Natural disaster mitigation has many benefits; improved community safety and resilience, a reduction in property damage, faster recovery, and reduction in the economic impact of natural disasters. There are a number of flood mitigation measures. These may be carried out by the state and its agencies (public mitigation works), or the property owner (private mitigation works).

It is NIBA's view that the current level of public flood mitigation activity is insufficient to adequately decrease flood risk. A 2014 Productivity Commission report into national disaster funding arrangements stated that governments "over-invest in post-disaster reconstruction and under-invest in mitigation that would limit the impact of natural disasters in the first place." A Deloitte report, also published in 2014, found that for every $10 spent on post-disaster recovery, only $1 is spent on mitigation. This is despite research released by the American Federal Emergency Management Agency (FEMA) which shows that $1 spent on disaster mitigation, saves society $6 in future disaster costs.

As communities begin to rebuild, we must not allow the mistakes of the past to be repeated. All rebuilding works must be undertaken with future disaster mitigation as one of the core focuses. This may include land buy-back programs to encourage affected residents to not rebuild in a flood-plain area or increasing building standards to include flood mitigation such as elevating buildings or flood-proofing parts of the building against water ingress. By doing so governments can reduce the economic impact of future events and the amount of future ex-gratia assistance provided to affected communities. Past inquiries have highlighted that current funding arrangements reduce the incentive for state and territory governments to invest in disaster mitigation as the federal government shoulders most of the burden for disaster recovery.

Public mitigation options may include both structural and non-structural measures, for examples building standards, land-use planning, dams, levees, floodways, and early warning systems. Previous mitigation programs have shown that both public and private mitigation works have a positive impact on home building insurance premiums.

In Northern Queensland, the Household Resilience Program, provides grants to homeowners for the purposes of undertaking cyclone resilience works to their property. These works can include roof replacement, installation of cyclone shutters or roof tie down systems and replacing of external doors. On average, homeowners

that participated in this program saved over $300 on their insurance premiums. Following devastating flooding in 2012 Roma undertook widespread flood-mitigation works, including the construction of a flood levee and a diversion drain. Following the completion of these works, the flood risk level for more than 500 properties was downgraded.

While NIBA believes that the most efficient way to reduce insurance affordability is through the abolition of inefficient taxes and levies, where premiums are high due to increased risk of natural disasters mitigation programs are effective in reducing risks and consequently lowering premiums. Improving affordability removes barriers to insurance and enables more homeowners to appropriately manage their risks.

Land-use planning

Land-use planning is another way governments can help to mitigate flood risk, by controlling where home and businesses are built. While it may be too late for homes that have already been built it is vital that land-use planning arrangements are amended so that no new homes are allowed to be built in floodplain areas.

NIBA also supports calls for homeowners and potential buyers to have greater access to climate property modelling to ensure owners and potential buyers can make informed decisions.

In addition to determining where homes are built, land-use planning can have a significant impact on insurance affordability. According to data collected by insurers the percentage of policyholders who made a claim and also have flood cover is lower in LGAs with high flood risk than in LGAs with lower flood risk. For example, in Lismore the percentage of policyholders who made a claim related to the March flood event and who also have flood cover is 31 percent, in Ipswich that figure is 69 per cent.

Conclusion

Insurance premiums ultimately reflect the level of risk of an individual property. For those who live in areas with higher flood risks this means that flood cover can often be prohibitively expensive even before the impact of insurance-based taxes and levies is taken into consideration. This means that those who most require insurance are often the most likely to be under-insured or have no insurance at all.

Governments can play an important role in reducing the underlying risk by introducing more effective land-use planning controls, investing in public mitigation, and providing grants for private mitigation works and finally, removing inefficient insurance-based taxes and levies that significantly contribute to the unaffordability of premiums and the resulting increase in levels of underinsurance and noninsurance.

Should you have any queries or wish to discuss any of the issues in this submission raised please do not hesitate to contact me or my office.

Yours sincerely,

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