



NATIONAL INSURANCE BROKERS ASSOCIATION (NIBA)

RESPONSE TO NATURAL DISASTER INSURANCE REVIEW - INQUIRY INTO FLOOD INSURANCE AND RELATED MATTERS

ABOUT NIBA

NIBA is the voice of the insurance broking industry in Australia. NIBA represents 500 member firms and over 2000 individual qualified practising insurance brokers (QPIBS) throughout Australia.

Over a number of years NIBA has been a driving force for change in the Australian insurance broking industry. It has supported financial services reforms, encouraged higher educational standards for insurance brokers and introduced a strong independently administered and monitored code of practice for members. The 500 member firms all hold an Australian financial services (AFS) licence under the Corporations Act that enables them to deal in or advise on risk insurance products.

EXECUTIVE SUMMARY

The review is an important opportunity to focus on identifying appropriate measures to achieve a nationally consistent, effective and sustainable response to disasters in Australia.

Like the Council of Australian Governments (**COAG**) NIBA is of the view that there is a need for “a whole-of-nation resilience-based approach to disaster management, which recognises that a national, coordinated and cooperative effort is needed to enhance Australia’s capacity to prepare for, withstand and recover from disasters.”

NIBA believes that the solution is not to focus on the insurance industry as proposed and the solution must involve a true combination of:

- Federal/State Government/local council initiatives; and
- private sector and consumer initiatives, including insurance cover.

With the above in mind, as an alternative to the models proposed in the review, NIBA proposes a **Combined Approach Model**, which comprises:

- *actual, identifiable and monitored mitigation efforts by Government*. In particular:
 - publicly funded and centralised flood mapping should be made available to better identify risks to consumers.
 - disaster standards should be required rather than being discretionary guidelines. For flood, a consistent national land use planning policy to reduce the number of flood



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exposed properties and changes to the Building Code of Australia to apply certain minimum standards relevant to natural hazards are worth considering.

- appropriate funds should be dedicated to preventative infrastructure projects including levees, barrages, flood gates and improved drainage etc.
- Government should consider removal of existing inequitable insurance taxes and communication of this may serve to encourage greater take up of insurance. The possible tax deductibility of insurance for certain high risk persons is also worth considering.

NIBA believes that the above would be likely to act as an incentive to the insurance industry to increase offers of cover and reduce price for the majority. The insurance industry's reaction to such initiatives should of course be monitored carefully to ensure the benefits are in fact passed on.

- *better education of consumers by Government as to the risks and insurance options that are available.* For example, obligations could be imposed on government and in particular local councils, regarding the disclosure of flood risk and promotion or provision of information regarding risk mitigation options to property owners and tenants. The value of obtaining personal advice to assist in risk mitigation should be promoted.

NIBA believes that this would be likely to result in:

- better individual mitigation of flood risks.
- a reduction in under/non insurance (which is a real issue of concern) that reduces the burden on the public and increase the premium pool which in turn would be likely to ultimately help reduce insurance cost. NIBA is concerned that compulsory flood cover from insurers and subsidies may not necessarily achieve this if the end result would be to increase the cost of insurance for the majority.
- a reduction in disputes as consumers better understand the cover they have obtained and the issues involved in flood claims.
- a market incentive to offer better cover as educated consumers will turn to those insurers providing the more comprehensive coverage and thus affect market behaviour.



- *the following industry changes:*
 - improved customer education regarding flood and the relevant risks. The standard flood definition and Key Facts Statement (KFS) initiatives of Government will assist in this. Consideration should be given to requiring insurers to clearly disclose whether a policy provides flood cover or not and any significant limits that may apply.

NIBA believes that better disclosure and education of the risks and cover would be likely to cause a shift to those insurers offering the relevant cover and increase the current market trend towards providing such cover. This may lead to some insurers seeking to obtain a commercial advantage by changing their stance through amendment of contractual terms as consumers become better educated and advised.
 - development of initiatives designed to avoid the claims issues that adoption of a standard definition will not address (i.e. is it flood that was the “real or effective” cause of loss and the operation of the Wayne Tank principle where there are concurrent causes of loss i.e. mixing of flood waters and storm waters where flood is excluded and storm is covered). For example:
 - independent expert (e.g hydrologist) binding both parties on such flood issues in cases of disasters.
 - a legislative provision overriding the Wayne Tank principle in relation to home building and home contents policies e.g applying a “pro-rata” payment so insureds are not left without cover.
- *appropriate Government subsidisation of certain high risk individuals for which flood cover would be unavailable.* Any funding/subsidisation model introduced must not have any material detrimental impact on the current insurance market, those not subject to flood risk and the incentive to mitigate.

One concept NIBA believes is worth considering, is a government fund for high risk consumers that provides a minimum level of flood protection. This could be linked to the consumer having to obtain home insurance which would work towards changing the under/non insurance problem currently faced. Some form of Government subsidy may also be provided for the premium of identified high risk insureds. Any such model should operate in a clear and transparent manner, with minimal moral hazard, and in a manner that gives the best protection to property owners according to the circumstances of their risks.



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NIBA RESPONSE TO DISASTER REVIEW GENERALLY

In December 2009 the Council of Australian Governments (**COAG**) acknowledged the need for “a whole-of-nation resilience-based approach to disaster management, which recognises that a national, coordinated and cooperative effort is needed to enhance Australia’s capacity to prepare for, withstand and recover from disasters.”

The National Emergency Management Committee (**NEMC**) subsequently developed the National Strategy for Disaster Resilience which was adopted by COAG on 13 February 2011. It currently provides high-level guidance on disaster management to federal, state, territory and local governments, business and community leaders and the not-for-profit sector.

NIBA agrees with COAG that if all these sectors work together with a united focus and a shared sense of responsibility to improve disaster resilience, they will be far more effective than the individual efforts *of any one sector*.

NIBA is concerned that the current proposals in the National Disaster Insurance Review regarding flood focus too much on the insurance industry and an insurance solution. Whilst it is part of the solution it is not the sole solution.

The National Strategy clearly and usefully sets out what is required of Government. NIBA believes the industry can and should work with Government and consumers to achieve the relevant goals.

NIBA has identified below in relation to each of the National Strategy goals, what it believes could be undertaken in relation to the flood disaster risk:

- develop and implement effective, risk-based land management and planning arrangements and other mitigation activities.

At a high level it is crucial that real and identifiable steps be taken by Government in relation to mitigation that can be properly monitored. This in turn is likely to allow the insurance industry to increase cover offered and better price it.

For flood this could include:

- *the development by Government of a consistent national land use planning policy that works towards reducing the number of flood exposed properties.*

Good work has been done in relation to bushfires already. For example, in NSW, risks associated with bush fires are regulated under the Rural Fires Act 1997. Under Division 8 of that Act, there is a legislative framework for land use planning and



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controls which mandates the assessment and control of bush fire hazards in land use planning and development.

In NSW, risks associated with flooding are not regulated, but are the subject of mere guidelines jointly published by the Department of Planning and the Department of Natural Resources. Recent events have shown that people die from flood events, just as they die from bush fires and the major risk of damage to private and community infrastructure from both types of events is also essentially the same. NIBA queries why one is regulated by a strong legislative framework, and the other is fully devolved to local councils with mere guidelines issued by the State?

- modernising the Building Code of Australia to include minimum standards for the durability of property that is subject to natural hazards. e.g ensuring the floor level is higher than any expected flood.*
- appropriate allocation of funds dedicated to preventative infrastructure projects including levees, barrages, flood gates and improved drainage.*

As the review notes, a good example of the value of such initiatives is where Lismore, built a flood levy for approximately \$19 million and a year after its completion had a one-in-10-year flood event. The town was protected by the levy and saved an estimated \$15m in damages. There are numerous other examples of the value to the community such Government mitigation funding can have.

Not all mitigation need be expensive. For example, the risk of flooding in Brisbane is already mitigated (to a degree) by the Wivenhoe Dam. There is a clear opportunity by way of proper management of the dam and the controlled release of water to further minimise the risk of flooding at little additional cost.

Such initiatives, whilst difficult, are a key part of the long term solution. Such measures would also increase the insurance industry's ability to price risk accordingly in flood-prone areas, which is currently affected because of a lack of flood mapping data and state-funded mitigation programs. Government could monitor industry response to such initiatives to ensure reduced risk is in fact taken into account.

NIBA notes that the review states that under its model "Allocating the task of funding to State governments would provide an incentive to mitigate the damage. State governments would be expected to seek to pass on the cost to State taxpayers and so would face an added incentive to undertake mitigation expenditure aimed at reducing future imposts on



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taxpayers.” NIBA does not believe this is likely to have the same effect as direct obligations imposed on Governments and councils regarding mitigation.

- have effective arrangements in place to inform people about how to assess risks and reduce their exposure and vulnerability to hazards.

In relation to flood, publicly funded and centralised flood mapping could be made available by the Government to the community. Currently there is no such mapping other than the National Flood Information Database created by the ICA which identifies properties with a flood risk according to publicly available Government flood mapping.

Centralised flood mapping could be combined with obligations regarding the disclosure of any flood risk and possibly promotion or provision of information regarding risk mitigation options to property owners and tenants when buying property or entering into leases or in rate notices, so as to promote their own risk mitigation strategies e.g identifying a flood risk in rate notices or other documents is likely to help promote the take up of insurance for such risks. The possible provision of incentives in appropriate scenarios should also be considered to promote individual mitigation activities by such persons.

The Government proposed standard flood definition and Key Facts Statement (KFS) is also likely to assist in education and assessment of the risk. See NIBA’s submission on standard definition provided to Treasury for its comments in this regard.

The value of obtaining personal advice provided by Australian Financial Services Licensees such as insurance brokers and other authorised persons should also be promoted. Any proposal by product issuers to allow for a more limited form of personal advice should be considered very carefully to ensure insureds are not led to believe they are getting more than limited advice and are properly informed of what the impact of such limited advice will be. Limited advice on limited risks will be of limited value and unless this is made clear, any such initiative has the potential to create issues in relation to risks not addressed in the limited advice. There is no substitute for the provision of comprehensive personal advice from qualified advisers such as insurance brokers.

Government removal of inequitable insurance taxes and communication of this may also serve to encourage greater take up of insurance by the community (see recommendation number 79 of the Henry Tax Review to abolish all insurance taxes, including fire services levies).

Industry must also play a role. For example, by:



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- *providing customers with access to flood mapping data available from the Government and links to other Government disaster initiatives or risk analysis tools.*
- *improving customer education regarding flood and the relevant risks. A standard definition of flood used by insurers and KFS will assist in this regard. Disclosure by insurers of whether a policy provides flood cover or not and any significant limits that may apply in the KFS would be useful in ensuring consumers are aware of the significance of the risk and allow them to move to insurers that provide the right level of cover. In combination with Government education, this is likely to influence market offerings by insurers and increase the number of insurers offering flood cover.*

- have clear and effective education systems so people understand what options are available and what the best course of action is in responding to a hazard as it approaches

In relation to flood, much of the above would contribute to this goal.

- support individuals and communities to prepare for extreme events.

Federal and State Government and local councils will have to play a significant role in this regard. NIBA notes that the General Insurance Code of Practice and Insurance Brokers Code of Practice both have disaster response provisions requiring cooperation of members. The Financial Ombudsman Service (FOS) external dispute resolution scheme that insurance brokers and insurers belong to also has procedures designed to prioritise disaster type scenarios.

- ensure the most effective, well-coordinated response from our emergency services and volunteers when disaster hits.

Federal and State Government and local councils will have to play a significant role in this regard.

- work in a swift, compassionate and pragmatic way to help communities recover from devastation and to learn, innovate and adapt in the aftermath of disastrous events.

Federal and State Government and local councils will have to play a significant role in this regard. The introduction of annual reporting by the Productivity Commission on the effectiveness of State and Federal disaster relief payments would also assist in the above.



NIBA notes that the General Insurance Code of Practice and Insurance Brokers' Code of Practice both have disaster response provisions requiring cooperation of members. FOS also has procedures that allow for faster resolution of disputes in exceptional circumstances.

NIBA notes that the next steps of the Strategy are to include NEMC developing a national implementation plan. It is expected that state, territory and local governments will use the Strategy to inform local action.

NIBA believes that development of such a plan should be given a high priority and consideration be given to imposing requirements (rather than guidelines) where possible to ensure mitigation is properly progressed (see NIBA's comments above on bushfire vs flood arrangements in NSW as an example).

NIBA is happy to liaise and participate where required in relation to the development of the plan. Given its members' risk management expertise, NIBA believes it will be able to contribute usefully to any such plan.

NIBA RESPONSE ON SPECIFIC FLOOD PROPOSALS

According to the review:

- “there are probably only about 50,000 homes subject to high flood risk, less than one per cent of Australia's estimated 6.2 million homes... [and] ... there are probably a further three to six per cent of properties subject to modest flood risk.”
- “For homes exposed to minimal flood risk, the market has been developing over recent years and more insurers are now preparing to extend the availability of flood cover, partly as a result of the stimulus of the recent events in Queensland and Victoria”

NIBA agrees with the review that for homes exposed to a high level of flood risk flood cover availability will always be problematic in a private insurance market. However, NIBA believes this is as much to do with the fact that there is no comprehensive Government focus on risk mitigation as the insurance industry's desire to not underwrite such high risks.

Whilst NIBA applauds the aim behind the review options, NIBA is concerned that automatic flood cover (with or without any opt out option) may not be an appropriate solution for the following reasons:

- there is no evidence of any general insurance market failure regarding flood. NIBA understands that:
 - 54% of policies currently provide cover with this trend increasing as a result of the recent QLD Flood experience. The Government initiative to develop a standard



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definition of flood and better disclosure by insurers in the KFS will also assist the process.

- A high percentage of claims lodged with ICA member insurers as a result of the Queensland and Victorian floods have been accepted.
- Assistant Treasurer Bill Shorten recently announced that almost 99% of claims arising from the Queensland floods have been responded to by their insurers. His main issue was that the rate of disputes for flood claims was “unacceptably and substantially higher than for other natural disasters”. Only the automatic cover option with no opt out would address such an issue. Other initiatives could be implemented to address this problem which NIBA notes in its proposed Combined Approach model below.

NIBA believes that the key issues are:

- affordability in high risk areas
- clarity in communication regarding what is and is not covered (in particular by insurers)
- consumer education to assist in understanding the risk and what is appropriate cover
- improvement in claims and dispute management for flood.

NIBA believes that its proposed Combined Approach Model discussed further below can address the above issues without the market ramifications that the automatic cover models may have.

- removal of any choice on whether an insurer should provide flood cover is not supported by NIBA as it may:
 - cause the exit from the market of some insurers, thereby reducing choice and competition for those without the need for flood risk cover. Insurers that currently do not offer the cover would have to implement new systems to offer the cover. They may not wish to do so and could simply exit the market depriving insureds without any flood risk of what may in fact be a very competitive cover appropriate for their needs.
 - result in increased insurance and other costs (i.e. rate increases) for the majority for the benefit of a few living in high risk areas. This in turn runs the risk of giving rise to an increase in non insurance/underinsurance. The Australian recently reported that according to RBS analysts, the costs of the recent natural disasters could translate into "personal and general insurance increases of up to 5 per cent". Some insurers have reportedly indicated the possibility of increasing home insurance premiums by



up to 10%. The implementation of the proposed models would only add to the pressure to increase costs.

- act as a disincentive for Government to mitigate the flood risk. Whilst the review has referred to foreign scheme models, NIBA notes that the UK scheme for flood insurance is reportedly at risk of failure as a result of Government mitigation failure and the US National Flood Insurance Programme scheme is apparently running at a significant deficit. Any relevant shortfall will most likely be recouped from the community.

- NIBA believes further detailed work needs to be undertaken in relation to the proposed Flood Pool and any other funding options that are identified as part of the current round of consultations, in order to ensure that a funding model can be introduced which will provide the desired level of protection and support to property owners in flood prone areas, but which will not have any material detrimental impact on the current insurance market. Any such model should operate in a clear and transparent manner, with minimal moral hazard, and in a manner that gives the best protection to property owners according to the circumstances of their risks.

NIBA does not support the maintenance of the status quo in the insurance industry as it will not address the issues that currently exist, namely:

- the need for improved and effective Government flood mitigation measures
- the need for improved consumer education to assist in understanding the flood risk and what mitigation steps are appropriate
- the lack of insurance affordability in high risk areas
- the issues regarding clarity in communication regarding what is and is not covered in particular by insurers
- underinsurance/non insurance issues
- the need for improvement in insurance claims and dispute management for flood claims.

PROPOSED NIBA COMBINED APPROACH MODEL

NIBA supports a Combined Approach Model which encompasses:

- actual, identifiable and monitored mitigation efforts by **Government**. In particular:



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- publicly funded and centralised flood mapping should be made available to better identify risks to consumers.
- disaster standards should be required rather than being discretionary guidelines. For flood, a consistent national land use planning policy to reduce the number of flood exposed properties and changes to the Building Code of Australia to apply certain minimum standards relevant to natural hazards are worth considering.

NIBA notes that the next steps of the COAG National Strategy are to have the NEMC develop a national implementation plan. It is expected that state, territory and local governments will use the Strategy to “inform local action”. NIBA believes that development of such a plan should be given a high priority and requirements rather than guidelines should be imposed where possible to ensure mitigation is properly progressed (see NIBA’s comments above on bushfire vs flood arrangements in NSW as an example of the disparity in approaches).

- appropriate funds should be dedicated to preventative infrastructure projects including levees, barrages, flood gates and improved drainage etc.
- Government should consider removal of existing inequitable insurance taxes and communication of this may serve to encourage greater take up of insurance. The possible tax deductibility of insurance for certain high risk persons is also worth considering.

NIBA believes that the above would be likely to act as an incentive to the insurance industry to increase offers of cover and reduce price for the majority. The insurance industry’s reaction to such initiatives should of course be monitored carefully to ensure the benefits are in fact passed on. The insurance industry should be closely involved in the COAG National Strategy process.

- better education of consumers by **Government** as to the risks and insurance options that are available. For example, obligations could be imposed on government and in particular local councils, regarding the disclosure of flood risk and promotion or provision of information regarding risk mitigation options to property owners and tenants. The value of obtaining personal advice to assist in risk mitigation should be promoted.

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likely to ultimately help reduce insurance cost. NIBA is concerned that compulsory flood cover from insurers and subsidies may not necessarily achieve this if the end result would be to increase the cost of insurance for the majority.

- a reduction in disputes as consumers better understand the cover they have obtained and the issues involved in flood claims.
- a market incentive to offer better cover as educated consumers will turn to those insurers providing the more comprehensive coverage and thus affect market behaviour.
- the following **industry** changes:
 - improved customer education regarding flood and the relevant risks. The standard flood definition and Key Facts Statement (KFS) initiatives of Government will assist in this. Consideration should be given to requiring insurers to clearly disclose whether a policy provides flood cover or not and any significant limits that may apply.

NIBA believes that better disclosure and education of the risks and cover would be likely to cause a shift to those insurers offering the relevant cover and increase the current market trend towards providing such cover. This may lead to some insurers seeking to obtain a commercial advantage by changing their stance through amendment of contractual terms as consumers become better educated and advised.

- development of initiatives designed to avoid the claims issues that adoption of a standard definition will not address (i.e. is it flood that was the “real or effective” cause of loss and the operation of the Wayne Tank principle where there are concurrent causes of loss i.e. mixing of flood waters and storm waters where flood is excluded and storm is covered). For example:
 - independent expert (e.g hydrologist) binding both parties on such flood issues in cases of disasters.
 - a legislative provision overriding the Wayne Tank principle in relation to home building and home contents policies e.g applying a “pro-rata” payment so insureds are not left without cover.
- appropriate **Government** subsidisation of certain high risk individuals for which flood cover would be unavailable. Any funding/subsidisation model introduced must not have any material detrimental impact on the current insurance market, those not subject to flood risk and the incentive to mitigate.



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One concept NIBA believes is worth considering, is a government fund for high risk consumers that provides a minimum level of flood protection. This could be linked to the consumer having to obtain home insurance which would work towards changing the under/non insurance problem currently faced. Some form of Government subsidy may also be provided for the premium of identified high risk insureds. Any such model should operate in a clear and transparent manner, with minimal moral hazard, and in a manner that gives the best protection to property owners according to the circumstances of their risks.

NIBA RESPONSE TO SPECIFIC REVIEW QUESTIONS

Given NIBA's proposal, it has not responded to all of the specific questions raised in the review. NIBA is however be prepared to engage in further discussion of such issues once consideration has been given to alternate models and believes interactive discussion of such issues is likely to be more valuable.