Andrew Barr MLA
Chief Minister

Member for Kurrajong

Treasurer
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Senator Chris Ketter
Chair
Senate Economics Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Senator ~~Ketter~~ Chris

Thank you for your email of 28 November 2016 regarding the Inquiry into Australia's general insurance industry and inviting my government to make a submission to this inquiry.

The ACT Government has been concerned with the cost and affordability of general and life insurance and the potential risk for under-insurance or non-insurance.

To that end, I am pleased to advise that the ACT has abolished insurance duty. The ACT is the first jurisdiction to have completely removed this tax. At the time of the 2016-17 ACT Budget, the rate of duty on general insurance was 11 per cent in South Australia, 10 per cent in Victoria and 9 per cent in New South Wales and Queensland.

Prior to the ACT's tax reform, a 10 per cent duty was levied on all general insurance premiums and 5 per cent on life insurance. The abolition of insurance duty will assist households and businesses in the ACT to better afford the level of insurance cover they would prefer, and help reduce the level of under-insurance. For example, an ACT household paying $3,000 per year in insurance premiums will now save up to $300 each year.

In the context of abolishing duty on general and life insurance, the ACT's submission to the Inquiry focuses on the policies the government has implemented to improve the compulsory third-party insurance (CTP) scheme. Despite the ACT never levying duties on CTPI, since introducing competition in the ACT CTPI market in 2013, tangible improvements have been delivered, including affordability improvements to CTPI policies.

The attached submission provides information on the CTPI scheme that directly responds to the Inquiry's first three terms of reference – cost, competition and transparency in the car insurance domain.

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Thank you for the opportunity to share the ACT Government's views on this matter. Further information and details on the ACT's CTPI experience and the cost of the CPTI in the ACT is attached for your information.

Please feel free to contact my office if I can assist you further on this matter.

Yours sincerely

Andrew Barr MLA
Chief Minister
28 FEB 2017

ACT Submission to the Inquiry into Australia's general insurance industry

Background

The States and Territories (States) generally apply insurance taxes to various insurance products which are mostly levied on premiums. They include life, general and compulsory third-party (CTP) motor vehicle insurance.

State governments impose tax on top of the insurance premium, with the taxes generally imposed on insurance companies and passed on to consumers.

Currently a number of States impose insurance duty on:

- Life insurance — most States impose duty on the sum insured and on term or temporary insurance policies. South Australia imposes the duty on annual premiums;
- General insurance — most States impose a fixed rate of duty on premiums ranging from between 5% and 11% for insurable items such as commercial and domestic motor vehicle, home and contents, public liability and professional indemnity; and
- CTP motor vehicle insurance – the majority of States impose duty on CTP premiums. Victoria and Western Australia impose a single rate of duty on premiums. Queensland, South Australia and Tasmania impose a flat fee.

The Final Report of *Australia's Future Tax System* (AFTS Report) highlighted that Australia was considered to have high insurance taxes, both in comparison to the taxes imposed on other products and industries, as well as compared to other countries. The AFTS Report also noted that specific insurance taxes should be abolished given the impact that they have on the cost of insurance premiums and under-insurance or non-insurance, and the economic efficiency gains this would deliver.

The Australian Capital Territory (ACT) is the first State to have completely abolished insurance duty commencing 1 July 2016, which is consistent with the AFTS. At the time of the 2016-17 ACT Budget, the rate of duty on general insurance was 11 per cent in South Australia, 10 per cent in Victoria and 9 per cent in New South Wales and Queensland.

Prior to the ACT's tax reform, a 10 per cent duty was levied on all general insurance premiums and 5 per cent on life insurance. The abolition of insurance duty will assist households and businesses in the ACT to better afford the level of insurance cover they would prefer, and help reduce the level of under-insurance. For example, an ACT household paying $3,000 per year in insurance premiums will now save up to $300 each year.

In the context of abolishing insurance duty and the Senate Inquiry into Australia's general insurance industry (the Inquiry), the ACT has been able to assist commercial insurers in reducing the costs for home and strata insurance, in terms of the removal of insurance duty. However, providing home and strata insurance has not ordinarily been the role and responsibility of the States (not historically a government function), being left to the private market.

The ACT has never levied insurance duty on CTP insurance. However, CTP insurance is a function provided by States, whether offered either by the State, akin to a government body such as the Transport Accident Commission (TAC) in Victoria, or by private insurers, as occurs in NSW and the ACT.

'Getting a car on the road' is largely comprised of CTP insurance; car registration; and comprehensive/third party property insurance. Importantly, a large component of this cost is driven by CTP insurance. Indeed, in the ACT, CTP insurance is around 1.5 times the cost of registration for a passenger vehicle.

In this context, and the ACT Government's historical insurance functions, this response to the Inquiry focuses on the active steps undertaken to improve the ACT CTP insurance scheme in terms of matters relevant to Inquiry. This includes, for example, opening up the CTP insurance market to competition, and the benefits this has produced for motorists, such as ameliorating the increase in the overall cost of car insurance [compulsory third-party insurance (CTPI) and comprehensive / third party property insurance] in recent years.

Introduction

This submission provides information to the Committee in relation to the ACT CTPI scheme and the changes that have been made to improve competition and transparency in that market. Specifically, the information seeks to address the following areas identified in the Inquiry's Terms of reference, namely:

a) the cost of CTPI over the past decade in comparison to wage growth;

b) competition of CTPI in the ACT; and

c) transparency of the CTPI in the ACT.

ACT CTPI Scheme in context

The CTPI scheme in the ACT is regulated by the ACT Compulsory Third-Party Insurance Regulator (CTP regulator), an independent Territory authority established under section 14 of the *Road Transport (Third-Party Insurance) Act 2008* (CTP Act). The role of the CTP regulator is to regulate the CTPI scheme in the ACT in accordance with the key objectives of the CTP Act which include, *inter alia*, providing for the licensing and supervision of insurers; promoting competition for CTP premiums; and keeping the costs of insurance at an affordable level.

In relation to the latter objective, the CTP Regulator's function as specified in the CTPI Act include ensuring that premiums meet the fully funded test and are not excessive; and monitoring the efficiency of the CTP scheme to identify areas for improvement.

The ACT CTPI scheme is primarily a Common Law based system and is comparable to those schemes that operate in New South Wales, Queensland and Western Australia, although with important differences. The ACT Scheme differs from the CTP schemes in Victoria, Tasmania and Northern Territory, which are largely no-fault schemes, where statutory benefits are available to those injured in a transport accident regardless of fault; and where Common Law damages may also be available for those not-at-fault, albeit subject to conditions.

The ACT scheme covers almost 300,000 registered vehicles in the ACT and offers Common Law settlement of treatment and rehabilitation costs in addition to economic loss and general damages. The ACT scheme design does not have thresholds to general damages, and caps [1] on some heads of damage.

[1] For example, Western Australia has significantly higher deductibles than other jurisdictions. This has the effect of making lower severity injuries ineligible for some payments. General damages have a minimum and maximum cap; in Queensland, general damages are based on a scale value of injury, so are effectively capped. However, in both jurisdictions, economic loss cannot be accessed where the plaintiff earns more than three time average weekly earnings. In NSW, for Common Law, claimants must have at least 10% whole body impairment to be eligible for general damages, and the amount is capped. In addition, the applicable discount rate for calculation in ACT

As the ACT scheme does not have any thresholds for access to Common Law (such as in the NSW and Queensland schemes), more claimants choose to access Common Law, and in turn a higher proportion of injured persons are able to utilise plaintiff legal costs. As a consequence, the proportion of claims payments on legal costs is higher in the ACT than in NSW and Queensland. The higher proportion of costs for general damages and legal costs also means a lower amount available for treatment and care costs, to the detriment of the recovery of those injured.

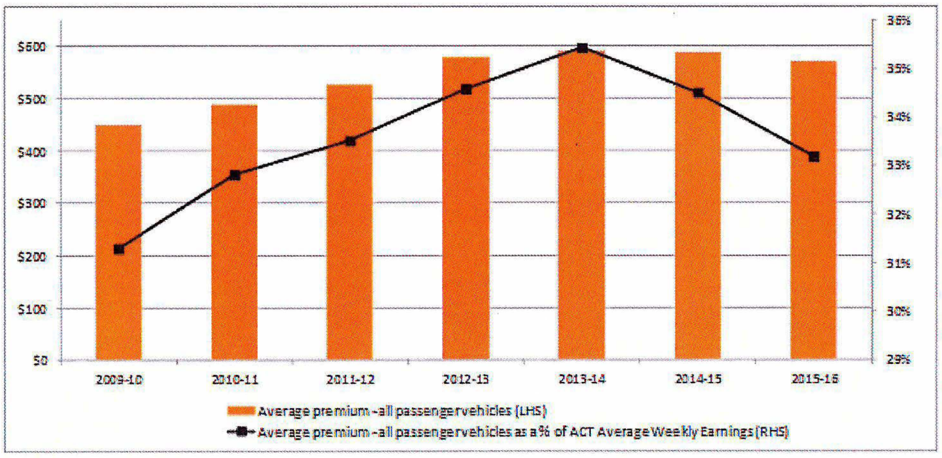
Response to ToR item (a) - The cost of CTPI in the ACT over the past decade in comparison to wage growth

Premiums and affordability

A key role of the CTP regulator is to keep the costs of insurance at an affordable level. The premiums charged by insurers to a large extent reflect the benefit structure underlying the ACT's CTPI scheme. As explained above, the ACT's scheme design differs from that of other State CTP schemes. The ACT arrangements are reflected in the higher premiums motorists pay in the Territory and hence impacts on the relative affordability of the scheme.

Affordability measured as premiums as a proportion of ACT average weekly earnings, declined over the period 2009-10 to 2013-14. This reflects average premiums increasing at a faster rate than the increase in average weekly earnings throughout this period. However, affordability has improved in 2014-15 and again in 2015-16 in trend terms due to premium reductions as a result of the introduction of competition in the ACT CTPI scheme, which commenced in practice from July 2013. Since 2013-14 premiums charged by CTP insurers have fallen in both nominal and real terms.

Figure 2 – Average Premiums for Private Passenger Vehicles and as a Proportion of ACT Average Weekly Earnings



Other important drivers of CTP premiums in the ACT in recent years have been the introduction of the Lifetime Care and Support Scheme (LTCSS) and the relative stable CTP claims frequency.

Common Law is 3%, whereas other jurisdictions adopt 5% or 6% per annum. This has the effect of increasing the present value of awards, particularly for economic loss.

Lifetime Care and Support Scheme (LTCSS)

A notable feature of the CTP landscape in recent years was the commencement of the LTCSS for motor vehicles in the ACT from 1 July 2014. The introduction of this scheme reflected the ACT Government's commitment to the National Injury Insurance Scheme (NIIS), which was developed as a companion scheme to the National Disability Insurance Scheme (NDIS), and assists in defraying the costs of the NDIS.

The LTCSS provides treatment and care to those who have suffered catastrophic injuries through a motor vehicle accident, regardless of fault. The scheme represents an expansion of available benefits for motorists, particularly given the inclusion of at fault drivers that incur catastrophic injuries.

With the introduction of the LTCSS, claim size within the CTP scheme, and in turn premiums have reduced, as treatment and care costs for catastrophic injuries have been transferred from the CTPI scheme to the LTCSS, which is funded by a $35 levy on each CTP policy. CTP insurers are therefore not on risk for the treatment and care costs for all catastrophic motor accident injuries, which represents a significant portion of the total costs of a claim. CTP insurers are, however, still on risk where a claim may exist for economic loss or pain and suffering.

Average costs of claims and claims frequency

Claims frequency and average cost of a claim are important drivers of CTP insurance premiums. The higher the claims frequency and average cost per claim, the more funding insurers need to cover future claim payments and hence the need to set higher premiums.

Claims frequency is an important measure as it indicates the proportion of the Territory's motor vehicles that are involved in a motor vehicle accident. [2] The frequency of claims in the ACT decreased in 2015-16 relative to the period 2011-12 to 2014-15. For the CTP Scheme overall, claims frequency has remained stable within a fairly tight band over the 2011-12 to 2015-16 period, hovering between a low of 29 and a high of 39 (that is, 29 to 39 in every 10,000 motor vehicles were involved in an accident).

The average claim cost for any one year is difficult to interpret given that a financial year can be affected by payments for prior years. For example, in the case of 2015-16, the average claim size increased, largely due to several multi-million payments being made in the June quarter of 2016 for the 2011-12 and 2012-13 financial years.

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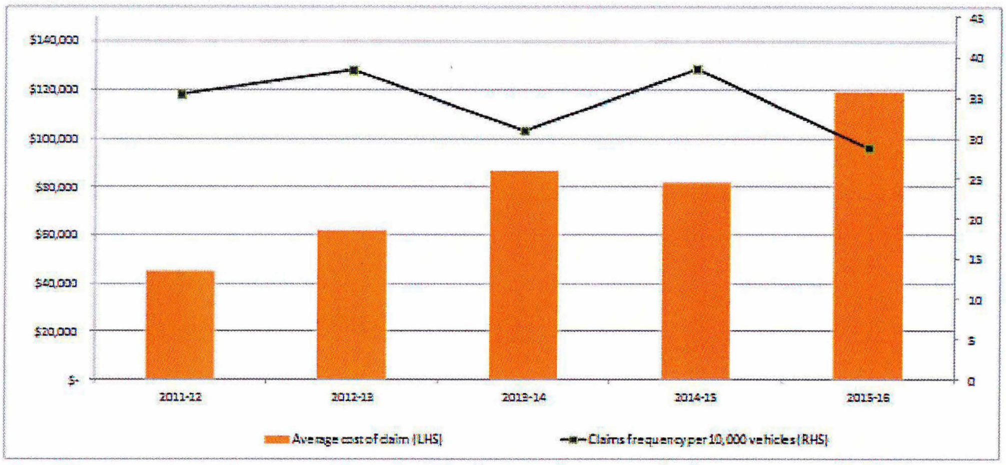
[2] Claims frequency is calculated by dividing the number of CTP claims by the number of registered vehicles.

Figure 3 – Average Claim Costs and Claims Frequency [3]



The CTP regulator has also been actively involved in road safety initiatives to reduce the frequency of claims and average claim size. In 2015-16 the CTP regulator contributed $75,500 to various road safety strategies aimed at mitigating third-party motor vehicles injuries in 2015-16. This comprised: $16,300 for a speeding initiative; $6,000 for a texting while driving initiative; $2,600 for a safer cycling initiative; and $26,000 for a driver distraction campaign.

The removal of LTCSS costs from the CTPI scheme; reduced premiums (see next section); and active road safety initiatives in combination with stable claims frequency, has assisted in reducing the ACT's average CTPI premiums relative to wages in more recent years.

Response to ToR item (b) - Competition in the ACT's CTPI scheme

One of the most significant changes in the ACT CTP environment over the last three years has been the introduction of competition.

The ACT Government established competition to, amongst other things: introduce innovative CTP insurance products; place downwards pressure on premiums; encourage more direct pathways to rehabilitation and treatment; and encourage a quicker return to health while obviating as many long-term injuries as possible.

CTP premium reductions

Competition has delivered reduced premiums to motorists and greater choice in product offerings – such as at-fault driver cover for motorists, and multi-policy offerings that provide discounts to premiums based on the number of policies and length of time held.

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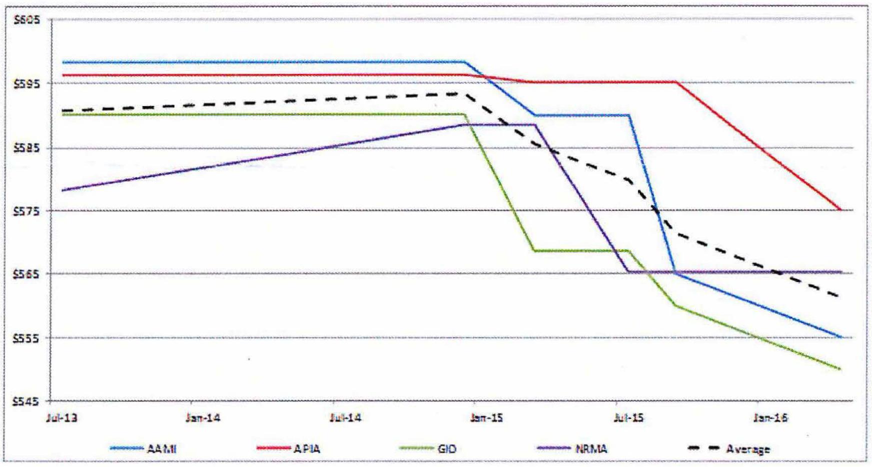
[3] *In deriving claims frequency, the number of claims are those added in the quarter and converted to a yearly basis, which are divided by the number of ACT registered vehicles with a CTP policy (excludes trailers and non-engine caravans / campervans).*
The average cost per claim is based on the payments made for the number of claims finalised in the quarter and converted to a yearly basis.

Since the successful introduction of competition to the ACT CTP insurance market commencing in July 2013, the three new entrants – AAMI, APIA and GIO – have cemented their position alongside NRMA insurance in the market.

In terms of premiums, motorists started benefitting from reductions in premiums in 2014-15, approximately 20 months after the Suncorp brands started offering CTPI premiums in the ACT market. Further reductions for all brands have ensued since then, as shown in Figure 4 below. Since competition commenced in the ACT CTPI market in July 2013 until 30 June 2016, the average private passenger vehicle premium has fallen by $29.43, or 5 per cent.

Figure 4 – Fall in CTPI premium prices since the introduction of competition



Competition to the ACT's compulsory third-party insurance scheme has delivered premium reductions to motorists, and at the same time, has led to a range of other benefits, such as at-fault driver cover and discounts on other insurance products held by motorists. This has assisted in ameliorating the extent of the increase in the overall cost of car insurance for motorists.

Impact of competition on market share

Information from insurers indicates that a significant proportion of motorists are changing CTP policies based on the premiums on offer at the time of renewal. This was reinforced by the findings of the 2016 review into ACT CTPI scheme which found that: "The ACT CTP market has exhibited considerable price sensitivity with relatively small reductions leading to increased market share for respective brands." [4] Figures 5 and 6 show the average market share for 2014-15 and 2015-16 respectively, based on premiums collected by insurers.

[4] Copy of the section 275 Review can be accessed on the ACT CTP Regulator's website http://apps.treasury.act.gov.au/compulsorytpi/ctp-publications

Figure 5 - Market Share over the 2014-15 financial year

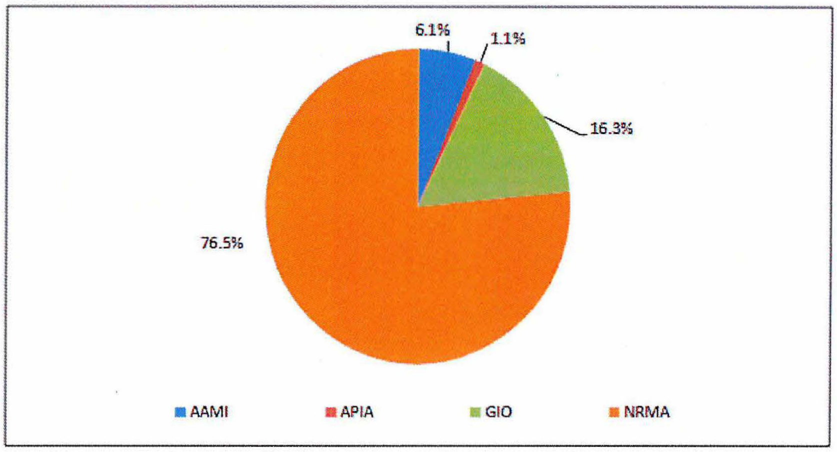
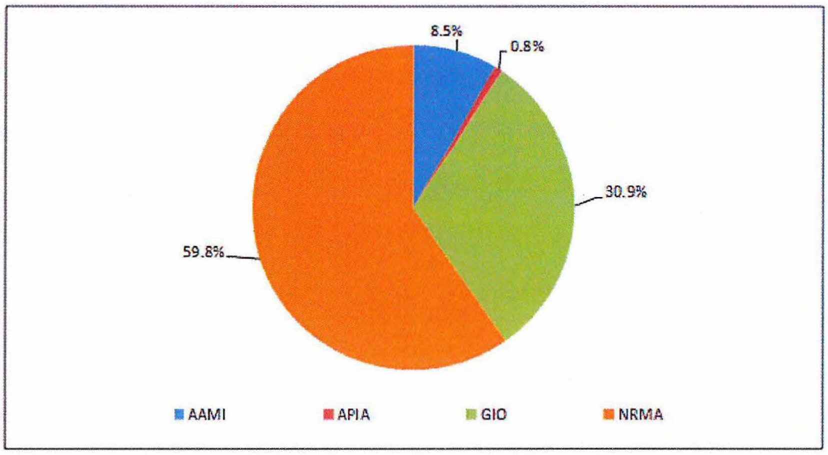


Figure 6 - Market Share over the 2015-16 financial year



During their second year of operation in 2014-15, Suncorp (GIO, APIA and AAMI) garnered a market share of 23.5per cent, up from an average of 10.2 per cent in the preceding year. NRMA held the balance of the market share with 76.5 per cent in 2014-15.

Over 2015-16, Suncorp's market share continued to increase, rising to a share of 40.2 per cent. NRMA's share declined to 59.8 per cent (a decline of 16.7 percentage points compared to 2014-15).

To date, the Government has been pleased with the benefits delivered by competition, including reduced premiums. However, it is expected that further reductions in premiums will be more difficult to achieve over time, and further premium reductions will be limited. This is reinforced by the findings in a recent review [5] of the operation of the CTP Act, which found that the ACT CTP scheme is being impacted by the scheme design, with few qualifying thresholds or caps on some heads of damage (such as pain and suffering). This is because the scheme structure has a strong effect on claim costs, which flows through to high premiums.

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[5] The Review of the operation of the CTP Act (Review report) was undertaken by the scheme actuary in accordance with section 275 of the CTP Act based on the claims and premiums experience over the 3 years to 31 December 2015.

As a result the Review report concluded that significant premium reductions in the future would require scheme reform.

Changes in market share for the CTPI insurers reflect a market responsive to CTP premium reductions. To date, this has encouraged competition around CTP pricing, and has led to CTP premium reductions. However, further reductions to premiums in the future are likely to be more difficult to achieve given the current design of the CTP scheme.

Response to ToR item (c) - Transparency in the ACT's CTPI scheme

Streamlining the CTPI scheme in response to competition

The CTP Regulator has undertaken a number of initiatives and improvements to the regulatory framework since the commencement of the introduction of competition to enhance transparency and the operation of the CTPI scheme.

Some of the enhancements include:

- providing market share reporting with statistics published in the Annual Report;
- highlighting and providing data in the Annual Report on the key drivers of CTP insurance premiums in the ACT, namely the average cost of claims and claims frequency;
- detailing the changes in CTPI premiums over time in the Annual Report, by insurer;
- highlighting and providing data on claims payments by heads of damage;
- revising the CTPI claims forms to reduce duplication and complexity;
- providing information to potential rideshare operators on the CTPI requirements when the new CTPI ridesharing class was created;
- overhauling the CTPI website to improve transparency and understanding of CTPI, including: providing information on competition and ridesharing; clarifying a range of terms associated with CTP insurance; introducing simpler and clearer steps to making a claim; and introducing new frequently asked questions (FAQs) to address common misnomers and recurring issues raised by the public; and
- promoting public awareness of the causes of motor accidents by financially supporting a range of road safety campaign initiatives.

In the interest of transparency of the ACT CTPI scheme, the ACT CTP regulator is required to publish the average annual risk premium for CTPI in the ACT. The risk premium represents the base risk amount that each insurer bears when providing CTPI in the ACT. The average risk premium price per policy is published each year by the CTP regulator in the Annual Report.

These improvements have resulted in a more efficient and transparent administrative process.

Clarifying motor vehicle insurance and the online quiz

During 2015-16, the CTP regulator conducted a short online CTP insurance quiz, consisting of a range of true or false questions that was available on the CTP insurance website from 18 April to 15 May. The quiz targeted more than 265,000 Canberra motorists aged 17-65.

The quiz was designed to gauge drivers' level of knowledge of the ACT CTP scheme and to improve, amongst other things, the understanding of the current arrangements, and importantly, the circumstances required to be eligible for CTP payments.

A total of 1,632 participants took part in the quiz with 79 per cent of participants answering five or more questions out of ten correctly. Despite the pass rate, the majority of participants (62 per cent) answered three to five answers incorrectly.

An analysis of the data (where there was a relatively high proportion of incorrect responses) shows that in general Canberra motorists lack knowledge about:

- the nature and meaning of an 'at-fault' system, and the need to prove fault in order to receive compensation;
- what a CTP policy covers in terms of insurance;
- the relative cost of the ACT's CTP scheme compared to other jurisdictions;
- the relative proportion of different payments by the scheme, including the relatively low proportion of scheme payments made for medical expenses for injured persons; and
- eligibility for the Lifetime Care and Support Scheme (when injuries are catastrophic).

Responses also highlighted a misunderstanding of CTPI and comprehensive car insurance, and that they were one and the same thing.

In light of the results of the quiz, the CTP regulator has developed strategies to enhance motorists' understanding of the features and benefits the scheme. Key strategies which have been developed include:

- revamping the CTP Regulator's website with a focus on enhancing public understanding of the CTPI claims process;
- developing an information booklet that explains how CTPI works, what it covers and does not cover and the benefits it provides; how your premiums are determined; and what happens with your premium dollars when you purchase CTP insurance; [6] and
- a fact sheet to explain the differences between the different types of vehicle insurance cover available on the market[7].

Streamlining the compulsory third-party insurance scheme to ensure it is better understood (including the linkages between the different types of compulsory and non-compulsory motor vehicle insurance offered), along with providing new and more information and access to online material, has improved the understanding and transparency of the scheme.

[6] The document "*Understanding Compulsory Third Party Insurance in ACT*" can be accessed on the CTP Regulator's website at http://apps.treasury.act.gov.au/__data/assets/pdf_file/0006/986424/Understanding_CTP_160909.pdf

[7] The fact sheet – How does motor vehicle accident insurance work in the ACT" is available on the CTP Regulator's website at http://apps.treasury.act.gov.au/__data/assets/pdf_file/0007/986425/CTP-Diagram-160906.pdf