



Federal Budget Submission 2024

INSURANCE: The Market Failure of an Essential Service

Supported by 19 Chambers of Commerce
across Northern Australia (QLD, NT + WA)



TOWNSVILLE
CHAMBER

INTRODUCTION

For 141 years the Townsville Chamber of Commerce has been the independent voice for the Townsville business community. As a nonpolitical, membership-based organisation, the Townsville Chamber is focused on advancing the interests of members' and looking to grow future opportunities in the North. We work collaboratively with all levels of Government, other representative bodies, and public and private sector organisations.

The Townsville Chamber of Commerce welcomes the opportunity to present the Commonwealth Government with the following submission for the 2024-2025 budget.

INDUSTRY SUPPORT

As the market failure of insurance in Northern Australia is a problem faced by a wider geographical area than just Townsville, the Townsville Chamber of Commerce has spoken to a number of Chambers and Industry Groups to support the recommendations made in this submission. We are pleased to advise the following organisations are not only supportive of the recommendations but have also added content and feedback in relation to the issues faced by trying to get affordable insurance in their regions.

TOWNSVILLE
CHAMBER



Northern Territory
Chamber of Commerce



Insurance: The Market Failure of an Essential Service in Northern in Australia

OVERVIEW

This is the Townsville Chamber of Commerce (TCoC) second federal budget submission in relation to the unaffordable and or unattainable insurance in Northern Australia. Follow Townsville Chambers first submission in January 2021, the Federal Government announced and implemented the Re-insurance Pool for Cyclone and Flood Related Damage (RPCFRD). The Federal government must be commended for acting on the essential service that is insurance. While there has been some commentary about the effectiveness of the RPCFRD, the implementation was always going to take time.

This submission follows the release of the second ACCC Insurance Monitoring report in December 2023 and considers its findings.

INSURANCE IS AN ESSENTIAL SERVICE

A business or individual cannot operate in a free market in Northern Australia without insurance. It is a requirement:

- by a financier when borrowing money
- for an individual or business that provides goods or services at the legislated Australian Standards
- when renting a premise
- as part of standard procurement, supply, and grant funding contracts with Local, State and Federal Governments
- to operate a business legally in Australia in most industries
- to lawfully own or occupy specific types of buildings and public spaces.
- to import or export for trade and commerce.

- to comply with both State and Federal legislation

Insurance is not a choice. Any Australian that contributes to making this great country a better place must have insurance. The Australian Government's agenda for fair and equitable playing fields for all Australians currently does not exist in insurance. Insurance is not a product that is available in the open marketplace for consumer choice, it is a legislative requirement and financial pre-requisite. Insurance is an **essential service** to conduct business, to buy a home, or contribute in a meaningful way to the economy.

THE PRINCIPLE OF INSURANCE

Insurance is a very old concept: Basically, it means many people paying a little money create a bigger pool of money so that anyone who is unfortunate enough to suffer a loss is reimbursed financially for that loss.

Understanding this basic principle is essential is understanding how we have come to this point of market failure in Northern Australia. If an insurer or insurance markets can operate in an environment where they do not need to provide insurance due to a properties geographic location or the type of risk like Cyclone, Fire, Flood, Terrorism that it is exposed to, there will be failure points in the market. Not insuring particular geographical areas or specific events means more profit, at less cost, which is good for the insurance industry but supportive of a practice that is contrary to the fundamental basic principle of insurance to spread the cost of the risk of any single event across as many participants as possible. The ACCC Northern Australia Insurance Inquiry (NAII) identified large percentages of people and businesses' that were either under insured or had no insurance at all. Critical to these findings is reliable data and when people are not participating in the insurance market, the pool of money gets smaller and the viability of a sustainable insurance market weakness. This is a race to bottom for the insurance industry. When the delivery of an essential service is the basis for the business model, the principle underlying the service must be structured correctly via clear government legislation that provides a clear environment for business to operate. Government intervention is required to provide this environment. This was the

basis for our call for government intervention in 2021, via a Re-insurance Pool, however this was **only a critical first step**.

In 2021 Townsville Chamber highlighted that the Australian Government intervention into the insurance industry does have precedence, in 2003 an insurance pool was created because terrorism cover was removed following the September 11 attacks in America, the Australian government has since expanded the ARPC's remit to include Cyclone and Flood Related Damage.

MULTIPLE REPORTS

The ACCC's NAII in December 2019 does not address the definition of a market failure but suggests that even if there is not yet a market failure across the whole of the country, government intervention is still justified.

*"This has included considering the extent to which affordability and availability issues stem from market failures, other impediments to robust competition or underlying cost drivers. **Without market failure, government intervention to reduce premiums may still be justified on social equity grounds or in support of broader policy objectives**". (Page 145 of the NAII)*

The term "market failure" was used by Allianz in their submission to the NAII in 2019.

"While an unavailability of needed insurance would meet the technical economic definition of market failure, Allianz suggests that an effective market failure arguably exists if such insurance is out of reach to those who need it because they cannot afford to purchase it." (Page 6)

The NAII has identified that there was significant non-insurance taking place in Northern Australia due to unaffordable or unattainable insurance in 2019, this could be argued to have expanded into other geographical locations in Australia where clear market failures of an essential service exist. There must be an understanding that if there is a market failure and insurance unaffordable or unattainable, **the insurer of last resort is the Federal Government**.

A SOLUTION FOR A COMPLEX PROBLEM

The insurance industry is complex. That does not mean there is no solution, it means a real solution may not be a simple one. In 2021 the Townsville Chamber made 4 recommendations due to the complexities within the insurance industry and clearly articulated then that more than one of its recommendations would be required to create **parity** in the insurance market for Northern Australia. An environment must be created where there is not only a baseline for the essential service that insurance provides, but insurance at that baseline is affordable and healthy competition remains within the marketplace. With the RPCFRD currently being rolled out, it is now time to revisit the recommendations to ensure the RPCFRD meets its full objective. **The Objective is "premium price parity for all Australians"**.

Provided there is a combination of these recommendations the Townsville Chamber of Commerce believes the issue can be resolved and the goal of insurance parity is achievable.

RECOMMENDATION ONE

Amendments to the RPCFRP legislation and review date.

The Townsville Chamber of Commerce was fully supportive of expanding the remit of the ARPC to include Cyclone and Flood related damage. It was TCoC's first recommendation in its 2021 -2022 federal budget submission. We provided written responses to multiple consultation papers and requests and was hearted to see several of its recommendations in the final legislation, it also must be acknowledged that some of the final legislation did include clauses that we disagreed with, however the importance of the having the RPCFRD pass into law was a critical first step and Townsville Chamber congratulates and acknowledges this achievement.

One of the critical roles the RPCFRD can now play is recording and gathering data to provide trends from the insurance industry. This is a critical component that hasn't been available for areas like Northern Australia that have suffered from unaffordable and unattainable insurance for decades. The ACCC released it's second monitoring report in Dec 2023,

and while acknowledging there can still be improvement in data collection, the value of having a detailed annual report comparing the insurance trends in Northern Australia to the rest of Australia is a critical in achieving the goal of insurance premium parity in Australia.

Recommendations :

1: REVIEW DATE – Interim Review.

The original review period for the RPCFRD was 3 years, July 2025. This review date was set as the large insurer's had until December 2023 to join while smaller insurers had until December 2024. While we acknowledge the great frustration in Northern Australia about the cost of Insurance and cascading affected that it has on the everyday lives of the people living here, the review date was set to 2025 to ensure there was enough time for the effects of the RPCFRD to be felt by the market (for people to renew their annual premiums). If the review is bought forward, there has to be sufficient data and evidence to make changes that will reduce insurance premiums in Northern Australia. . The core objective of the RPCFLD is to create premium parity, this should be front and center of any decision on moving a review date. If there is evidence and data available for the review to be bought forward the TCoC recommends an "Interim Review" targeting specific parts of the legislation that will have the biggest effect of achieving the outcome of premium parity. The original 3 and 5 yr. reviews should be left in place as the timeframe aligns with the entry dates for insurers and allow for their premiums to be renewed under the new pricing. Below are recommendations of areas that could be targeted with the Interim review.

2: DURATION OF COVER AFTER CYCLONE EVENT ENDS

Section 1.46: The claims period ceases at a fixed time of 48hrs after the cyclone formally ends.

While Townsville Chamber provided a detailed submission on the issues of creating new definitions and timeframes clauses, the final legislation included a fixed time of 48hrs after a cyclone formally ends to cease reinsurance cover. Most Reinsurance catastrophe treaties define a standard event as lasting 7 days (168 hrs) while some have been identified that last up to 28 days (672hrs). This must not be confused

with the design of the RPCFRD as the time period of 48hr is after the event has ended. For example, a cyclone event could indeed and has in the past been off the coast and out at sea for a number of weeks before making landfall.

The basic function of the Reinsurance Pool is to create competition in the marketplace and drive insurance premiums down. The 48hr clause was modeled by treasury and some insurers have supported the 48hr period as the most sustainable for the RPCFRD while increasing competition and created premium parity.

Section 1.47 of the TREASURY LAWS AMENDMENTS (CYCLONE AND FLOOD DAMAGE REINSURANCE POOL) BILL 2022 does acknowledge that this 48hr period may need to be amended in the future to ensure the goal of insurance premium parity for Northern Australia.

The 48hr timeframe should be part of the interim review, with the end outcome being premium reduction and in turn RPCFRD sustainability.

3: \$5M LIMIT FOR BUSINESS.

The Townsville Chamber has found examples in the North Queensland market where insurance is now not available above \$5 million for businesses. While the Townsville Chamber highlighted the issue of defining a business size by sum insured in earlier submissions this issue is starting to play out in the marketplace.

Insurance is an essential service, businesses need affordable and attainable insurance to operate freely, borrow money, employ staff and comply with their statutory obligations. When the Reinsurance Pool for Terrorism was created it didn't discriminate on total sum insured and this should be the same for the Reinsurance Pool for Cyclone and Flood related Damage.

These same commercial policy holders in Northern Australia have been paying between 2% and 5.6% on their premium since 2003 into the Reinsurance Pool for Terrorism, most unknowingly. While this is collecting a little from many to cover the losses of a few, it is indeed following the definition of insurance. According to the ARPC 2022-2023 Annual Report, the terrorism insurance scheme currently has \$14.4 Billion available for claims that arise from a terrorist attack and has customers with a sum insured value of approximately \$4 trillion nation-wide for commercial

property and business interruption. Businesses in northern Australia are being decimated because of a geographical location and are experiencing the same market failure experienced in 2002 for a terrorism event.

The other major issues with excluding policies over the set number is the insurer of last resort will be the Federal Government.

The \$5 million cap for businesses must be removed.

4: AGRICULTURAL PROCESSING

Townsville Chamber identified a problematic and unfair exclusion that impacts the agricultural industry in Northern Australia. Where buildings that are on the same property as crops are being grown are not covered by the pool.

Section 7 – A contract is not a pool insurance contract to the extent that:

7 b(ii) Secondary processing of, or manufacturing of goods from, the crops, livestock or produce, at the place where the crops or livestock are produced and

Exclusion 7b(ii) should be removed from the exclusion provision of the RPCFRD. This is a disincentive for a primary producer to value add to their product before the farm gate. Value adding, creating regional employment opportunities, and created sustainable supply chains is critical to not only Northern Australia but to the whole of Australia's future. Excluding the very thing that farmers have been encouraged to do for many years is counter intuitive.

RECOMMENDATION TWO

The obligation for an insurer to provide insurance for all of Australia.

As part of obtaining an insurance license in Australia retail insurance providers must provide products to cover every part of Australia. This system works in parallel to a reinsurance pool. The pool provides confidence for insurance companies to re-enter the market and competition is critical to ensuring any government intervention reaches its full potential.

Regionalising the profitability of insurance completely contradicts the definition of insurance. When the risk is spread over the whole of Australia, the profitability of the insurance industry is indeed healthy. An

estimated profit of \$8.2 billion from home, contents, and strata insurance in the rest of Australia, on a gross earned premium of \$69 billion, at a gross margin of 12% over the 12 years to 2018-19 is a healthy industry (See page 108 of the NAI). Singling out Northern Australia as one region that was not profitable, with a recorded loss of \$856 million or profit loss of 13%, does not mean insurance in Australia is not profitable, it just means you can indeed make more profit, and have less costs, if you are allowed to operate in just the profitable areas and not insure specific parts of Australia. As profit margins are pressured and shareholders require returns, multiple insurance companies are choosing to exit these areas.

If we continue to allow insurance companies not to spread the risk, insurance (an essential service) will become unattainable in Australia.

The ACCC's NAI has highlighted a problem that people in Northern Australian, and the insurance companies already knew existed. This report will escalate the problem of affordable and obtainable insurance in Northern Australia. In the long term, this will not be contained to Northern Australia if insurers are allowed to only insure in "safe" or "low risk" areas. By understanding the basic principle of insurance, it is clear that Australia is not being provided with the essential service that is required and Northern Australia is not insured to the standard that Australians require.

Removing cover from particular areas, either through geographical boundaries, postcodes, street names, or not providing cover for named events like cyclones, floods, or terrorist attacks, is not spreading the risk. Rather, insurance companies are eliminating their exposure via exiting the marketplace. The risk is not being spread across the entire country. The hard reality at the moment is Northern Australia is contributing to a reinsurance pool to address a market failure for terrorism which will most likely occur in major capital cities, but major capital cities are not contributing to risks faced by people living in Northern Australia.

To drive a competitive and robust market, the risk of insuring in Australia must be shared across the whole of Australia.

RECOMMENDATION THREE

National Insurer – Baseline of insurance for all Australians

There has been a market failure of an essential service in Northern Australia and if there is not a willingness from the private sector to provide affordable and attainable insurance to the entire country then there is no other option but for the Government to provide a baseline cover for the essential services required by legislation.

As a minimum, the standard cover should include “no frills” building and contents and public liability for properties. In the same way the Government delivers other essential services to Australians like health care, the private market can continue to operate and provide optional products and levels of choice coverage in healthy competition freely above the essential service baseline offered by the National Insurer.

As highlighted in the ACCC’s NAI, offering the baseline service would be profitable for the national insurer (as more policy’s would be taken out) and achieve the objectives of premium parity across Australia.

RECOMMENDATION FOUR

Abolish Additional Fees – Stamp Duty and GST

REMOVE STAMP DUTY

State Government based stamp duty on the essential service of insurance has received criticism from multiple agencies and is one of the leading recommendations from many looking at the issue of unaffordable and unattainable insurance in Northern Australia. **Stamp duty is applied to premiums amounts after the GST is applied, so a tax on tax.** In Northern Australia where premium prices are 2 to 3 times the national average, stamp duty can account for up to a 30% increase on a premium when trying to achieve premium parity. It must also be highlighted that the GST is distributed to the States via a mechanism called Horizontal Fiscal Equalization. While there is currently a transition to the 2018 GST legislated arrangements in the 23-24 year,

Queensland is still collecting more revenue from GST than it is creating, receiving \$1.03 for every \$1 of GST collected. Collecting Stamp duty on top of the GST allocation is double taxing and complete unjustifiable on the essential service.

It has been widely acknowledged that stamp duties on insurance products are an inefficient form of taxation. This recommendation is in line with recommendations from previous inquiries into insurance and taxation issues. Governments have previously received and continue to enjoy a windfall gain from the increase of insurance premiums in Northern Australia.

Stamp Duty must be removed from insurance premiums and the federal government may have to look at insuring this happens. The federal government is currently doing the heavy lifting and the state must do their share.

REMOVE GST

As an essential service (similar to fresh fruit, healthcare and bank account keeping fees) the insurance products should be GST free, whether nationwide or only in Northern Australia where there has been a market failure.

The direct impact on affordability of premiums for Northern Australia will be significant, exacerbated by the taxes applied, and the comparative loss of revenue for the respective governments would be negligible due to the population of Northern Australia and the extent of non-insurance and impending further decline of insurance participation.

It should be noted that removing State and Federal taxes without ensuring healthy competition in the marketplace will see these benefits disappear.

CONCLUSION

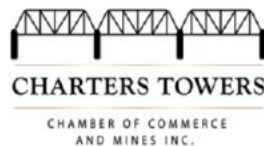
In the upcoming budget it is imperative that provisions be made in relation to building a competitive, robust, and sustainable insurance market in Australia.

A combination of the above recommendations is critical to ensure fair and affordable insurance premiums in Northern Australia.

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