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**Insurance Council Of Australia**

**Submission To The House Committee  
Into Recent Bushfires**

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### Introduction

The Insurance Council of Australia (ICA) is the representative body of the general insurance industry in Australia. ICA members account for over 90 per cent of total premium income written by private sector general insurers.

ICA members, both insurance and reinsurance companies, are a significant part of the financial services system. Recently published statistics from the Australian Prudential Regulation Authority (APRA) show that the private sector insurance industry generates direct premium revenue of \$19.8 billion per annum and has assets of \$66.6 billion. The industry employs about 25,000 people.

ICA members issue some 37.8 million insurance policies annually and deal with 3.5 million claims each year.

The IDRO was established in March 2000 to replace and upgrade the services provided by the Insurance Emergency Service which had been in operation since 1967. The IDRO and its predecessor have provided a facility for insurers to assist them in responding to natural disasters by providing a central interface point for insurers, Government, the community and the media.

In short, IDRO provides a streamlined framework for the industry's management of natural disasters under the auspices of the Insurance Council of Australia.

IDRO is itself a partnership of insurers, reinsurers, brokers, loss adjusters and Insurance Enquiries and Complaints Ltd (IEC), which are all, represented on a national committee reporting to the ICA.

During the summer of 2002/03 bushfires cut a swathe through several Australian States and Territories, unfortunately producing tragic consequences for many individuals and businesses.

We provide this submission based on:-

- The insurance industry's experience in dealing with natural disaster situations; and
- Our observations about the policy and administrative actions by Government and industry that best assist communities to minimise their exposures to bushfire emergencies while mitigating the tragic impacts of them.
- The Committee's terms of reference as it relates to general insurance.

Our submission is also framed with regard to the periodic reviews by State and Territory Governments and legislatures of their planning for bushfires and post event responses to them.

We are also mindful that a thorough public debate on these matters will also occur at the Third International Wildland Fire Conference to be held in Sydney in October of this year. This conference is expected to draw some of the world's leading authorities on wildfire management.

With a string of human tragedies occurring in recent times, tragedies that have been exacerbated by underinsurance and non insurance, ICA raises as part of this submission proposals to ease the burden of the cost of insurance on households and families by making the cost of home and contents insurance for a primary residence tax deductible while also easing the current insurance tax impost on all policy holders.

Our submission is comprised of six key sections:-

- Review of the 2002- 2003 disaster season;
- The role of the Insurance Disaster Response Organisation (IDRO);
- Effective disaster planning;
- Under Insurance and Non Insurance; and
- Insurance Taxes
- Conclusion and Recommendations

## **Review Of 2002 – 2003 Disaster Season**

Bushfire disasters occurred throughout NSW, the ACT and north-eastern Victoria from October 2002 to January 2003.

The bushfire season was particularly severe in late 2002 with significant impact by the El Nino climatic induced drought conditions coupled with high temperatures, low humidity and very strong westerly, south westerly and north westerly winds.

Fires in Engadine in October 2002 (11 houses destroyed, damage to 18 others) were followed by fires at Abernathy (9 homes), Ewingar (8 homes), Grafton (3 homes), Lake Macquarie (1 home), Willow Vale (6 homes), Copmanhurst (1 home), Glenorie (37 homes), Wattle Grove (4 homes) and Medlow Bath (2 homes).

In all 82 houses were destroyed between October and early December throughout NSW and an equal number were severely damaged. There were many other buildings either destroyed or damaged as well as some commercial and industrial loss. Industry estimates puts the overall loss at \$ 40 million.

The bushfires in the high country of NE Victoria and SE NSW throughout January and February 2003 have produced insured losses of some \$ 15 million. There were some 60 household, 143 farm and 5 commercial claims for an overall estimate of \$ 12 million in NE Victoria alone.

A very severe firestorm struck the western suburbs of Canberra on 18 January 2003, destroying 474 houses and damaging about 800 other domestic properties. Some 300 motor vehicles were destroyed and many others damaged. Also lost to these fires were a number of commercial and industrial properties and the Mount Stromlo observatory complex.

With the inclusion of the insured loss to the Stromlo pine plantation forest the overall insured loss estimate stands at \$ 345 million. This natural bushfire disaster stands second only to the Ash Wednesday fires of 1983 in Victoria and South Australia.

There has been a significant involvement of the Insurance Disaster Response Organisation (IDRO) in the response, recovery and reconstruction phases of the Canberra bushfires. The role of the IDRO in addressing disaster situations is discussed in detail below.

It is the considered view of the IDRO that particular recognition should go to the dedication and professionalism of our fire fighting services' paid professional employees and volunteers who, in many instances, risked their welfare to protect human lives and property during this and countless other bushfire seasons.

Bushfire and fire is a natural disaster where the community receives a high level of protection and mitigation services.

It is IDRO's clear view that bushfires would present a far greater threat to communities if not for the courageous work of these professionals and volunteers who work to keep bushfire loss to a minimum.

## **Role Of The IDRO**

The new structure of the IDRO recognises that the insurance industry has for some time embraced modern technology for claims and loss adjusting practices. In most disaster situations individual insurance companies and their claims management processes can cope with extensive numbers of claims.

The IDRO, on behalf of the industry, forms partnerships with all levels of government and with disaster affected communities. The aim is to bring an increasing awareness of everyone's role during natural disasters so that when a disaster does strike everyone is better equipped to deal with it.

## **Rapid Community Assistance**

A significant problem with large numbers of disaster related claims has been that they come from a community which may feel disempowered. People may have lost all their possessions; they may not want to leave their homes. The IDRO is designed to coordinate the industry so that it can work with government to provide the best possible response and recovery service for these people.

To achieve this IDRO provides a single point of contact in each Australian State and Territory to assist policyholders affected by the disaster. This may be by providing information on how to lodge a claim; giving general advice to those with possible insurance claims; and helping policyholders to identify their insurance companies if they have not already done so.

Natural disasters generate thousands of claims and while there is scope for insurance companies and loss adjusting firms to continue developing efficient coping strategies for dealing with a large number of claims there is always the overriding contractual obligation on the insurer to handle each claim on its individual merit.

However, the IDRO achieves some balance between individual assessment and claims settlement processes and the advantages that are gained through collaborative effort. IDRO does this by working with all of the government departments and agencies involved in disaster response such as the Premier's or Chief Minister's Department, the Office for Emergency Services, the Police Service, Fire Fighting Services and the State Emergency Services.

The IDRO also works with the Government's disaster recovery committees which include charitable organisations such as the Salvation Army, the St. Vincent de Paul Society, Anglicare, Adracare and the Red Cross etc.

### **Activation Of IDRO During Disasters**

When a State Government declares an event a disaster, the IDRO is automatically activated and takes its place on any committee or task force established by the relevant Government to ensure the insurance industry participates in and benefits from the whole of government approach.

New South Wales and the Greater Sydney Region in particular has been the target of the greatest number of natural disasters in recent years. Since 1993 this area of Australia has recorded over half of the total number of disasters for the whole of the country. As a consequence the IDRO has been more active in NSW than in the other states. Concomitantly, the NSW Government has been more involved with disaster response, recovery and renewal of affected communities than other Australian states.

### **Effective Disaster Planning**

When a very severe hailstorm struck Sydney on 14 April 1999 damaging some 22,000 houses and hundreds of commercial, industrial and public buildings as well as some 62,000 motor vehicles, the NSW Government reacted immediately to establish a whole of government approach to this major disaster.

The Government established the Southern Sydney Hailstorm Recovery Task Force which combined and coordinated all of the government and charitable organisation's response agencies as well as the building and insurance industries.

This whole of government approach was a spectacular success, most notably by reducing an anticipated reconstruction period from two years to six months.

The insurance industry was ready to join the government's task force from the outset. Although the IDRO was yet to be launched its design structure had already been agreed.

Rather than being a reactive organisation, activated only after an event has occurred, the IDRO is a pro-active organisation. It does this through ongoing communication with government at federal, state and local levels and with government response agencies. The same situation applies with scientific organisations, which have a focus on natural disasters such as Emergency Management Australia (EMA), Geoscience Australia and the Bureau of Meteorology.

The insurance industry wants to know as much as possible about natural hazards and the way governments and their agencies will respond to them. Similarly, governments need to know how

the insurance industry will respond, especially with specific types of hazards such as flood, where insurance coverage may not be sufficient across the whole of the flooded community.

**The Taskforce approach referred to above is now replicated whenever a disaster situation is declared in NSW. This model has also been adopted by other States as an effective and efficient approach to delivering urgent assistance to communities during disasters.**

If it has not occurred already, ICA would recommend that all State and Territories adopt a whole of Government taskforce approach, inclusive of relevant charitable organisations as well as the building (as appropriate) and insurance industries, as part of their State Disaster Plans. We would urge that this be a recommendation made as part of the House Committee inquiry's final report.

## **Community Response To Disasters**

Disasters come in all shapes and sizes and their impact on communities varies considerably. The IDRO's involvement with disasters over many years reveals that no two disasters are ever the same and flexibility is the key to a successful response.

Some communities are experienced with disasters, for example, communities which are exposed to regular flooding usually exhibit a high degree of resilience when flooding occurs. On the other hand many communities have very little expectation of disaster and suffer a high degree of trauma when struck by a sudden and unforeseen event.

Disaster experienced communities are usually prepared to recover from the event and from the insurance industry's perspective have a normal expectation of the claims processes that will reinstate their homes and businesses. Conversely, individuals confronting a natural disaster for the first time may replace the initial satisfaction they had with the response effort with dissatisfaction brought about by anger and frustration caused through their inexperience in dealing with insurance claims and loss adjusting personnel and the building industry.

It is with these less well-prepared communities that the insurance industry finds it must use every available means to help the affected people.

## **Insurer Preparation For And Management Of Disaster Claims**

In Australia, insurers prepare for the disaster season, October through March, to enable them to respond to an event which may produce thousands of claims but at the same time also be capable of processing everyday claims such as home burglary or motor accident.

Sometimes, several natural disaster events strike across a time span that puts enormous pressures on company resources. For example, the Newcastle earthquake of 28 December 1989 produced some 70000 claims for \$ 1124 million and took several years for all claims to be processed to completion. But during the span of this operation insurers had to respond to a hailstorm in Sydney on 18 March 1990 that produced 40000 claims for \$ 384 million and a thunderstorm again in Sydney on 21 January 1991 that produced 34000 claims for \$226 million.

Company management, in these circumstances, has to juggle claims and loss assessing resources and may at times be stretched to the limit. Similarly, companies are put under enormous pressure to cope with the increased flow of enquiries and claims.

The IDRO, and insurers individually, use the media to explain claim processes and bring to the attention of policyholders and the community generally, what is required to assist them with their claims. Many insurers have special strategies to advise their claimants on how they should go about making their claim and the responsibilities and obligations of both the insurer and policyholder to settle the claim to the satisfaction of both parties.

A number of insurers have adopted the concept of positive claims assessing by which they make contact with their policyholders to check on damage rather than wait on the insured to formally notify their claim. This practice is one of the benefits of modern technology whereby a company's database is geocoded enabling identification of insured properties inside the disaster zone.

From February 1967 through to January 2003 IDRO (and IES it's predecessor) have provided their services to the industry during 157 major disasters in Australia (**Appendix A**). Of those 157 major disasters involving cyclones, earthquakes, hailstorms, flood, storm and bushfires, bushfires accounted for just over 10% of these events at an equivalent current cost of \$1.062 Billion.

## **Underinsurance And Non Insurance**

The recent bushfires that have ravaged NSW, the ACT, Victoria, Western Australia, Tasmania and Queensland have demonstrated that the extent of underinsurance and noninsurance in the community remains high.

Recent research by ICA has found that up to one in four households in Australia carries no insurance at all, with this percentage being influenced by non insurance in the tenancy and housing commission sectors. Preliminary investigations by IDRO following the ACT firestorm has found (based on well over 100 households affected by the fires) significant underinsurance of contents, with underinsurance ranging between 30 and 50 percent below realistic replacement costs. House structures were found to be underinsured, on average, by 40 percent of the replacement cost.

Wherever natural disasters strike Governments are called upon to provide financial support to members of the community who do not hold adequate insurance.

In the case of the NSW and ACT bushfires, both governments have provided financial support to victims. In NSW cash grants of \$10,000, irrespective of a persons financial and insured status, were offered to those affected by the fires. It is understood that these grants were funded from the Community Disaster Relief Fund which is built from contributions provided by the NSW and Federal Governments, in addition to donations provided by the public. Victims can also access a separate grant of up to \$10,000, however, this payment is means tested and is strictly needs based.

In the ACT \$5000 has been offered to bushfire victims irrespective of their insured status with a further payment of up to \$5000 being available to uninsured people even though they may have deliberately chosen not to insure at all.

In addition to these payments if the State or Territory Governments have advised the Commonwealth of a natural disaster, individual victims can be eligible for payments of \$2000 each under the physical hardship and distress provisions of the Commonwealth's Natural Disaster Relief arrangements. These arrangements also see the Commonwealth contributing to the cost of rebuilding public infrastructure if certain loss thresholds are met by the State in which the natural disaster has occurred. These expenditures add up to a major financial outlay by Australian



Governments following on from natural disasters. A lot of this expenditure could be eliminated if people prudently insured their assets.

## **Insurance Taxes**

Some Australian States have world record taxing levels on insurance.

The insurance industry has long argued that the impact of the State and Federal taxes on insurance, which often amplify each other, acts as a major disincentive for people to prudently insure their assets to protect against a misfortune, natural or otherwise, that might befall them.

Some States are subject to the cascading effect of three taxes on a basic premium, a fire levy, then the GST followed by State stamp duty. The price disincentive of a 'tax on a tax on a tax' on general insurance products remains in the two largest and most populous States of NSW and Victoria while other jurisdictions continue to maintain stamp duty on insurance policies that add to and amplify the impact of the GST on basic premiums.

Enclosed at **Appendix B** are ICA tables showing the impact of State and Federal Taxes on both household and business insurance. By way of explanation, a hypothetical basic premium of \$100 is used to demonstrate the point about the huge taxation impost on these policies.

Australia's taxation treatment of general insurance products is in the same vein as the 'sin' taxes that apply to cigarettes and alcohol has resulted in our maintaining the highest level of insurance taxes in the world.

In rural Victoria, for instance, the combination of the triple tax impost on top of the insurance premium is as high as 77 percent which serves to penalise those in the community who choose to prudently insure.

## **State Moves Towards Insurance Tax Reform**

2002 did, however, see some States consider insurance tax reform. The WA Government passed legislation to reform its Fire Service Levy (FSL) to enable a more equitable system of funding its fire services to be established via local Council rates. In doing this the WA Government has recognised the inherent unfairness of requiring insureds to fund fire services that support the whole community. Unfortunately, however, the WA Government as part of its 2003/04 budget has announced an increase to its stamp duty rate on insurance from 8 percent up to 10 percent – a plan likely to wither savings to the insured public from the abolition of FSL.

Victoria is also considering its position on the FSL issue commencing an inquiry into its application in that State late last year. The Victorian review is due to report later this year.

In its 2002/03 budget the NSW Government decided to reduce the level of stamp duty it applies to general insurance products to 5 percent in response to community concern about rising premiums, fuelled by government taxes and the confluence of local and international events affecting the insurance industry.

The NSW Government, in response to the final report of the HIH Royal Commission, has announced its intention to examine alternatives to FSL in that State so that the funding of fire services is more fairly applied across the whole community. In the interim, NSW general insurance premiums, however, are still impacted by the triple taxation impost adding 50 percent to basic business premiums.

### **HIH Royal Commission Tax Reform Recommendations**

The HIH Royal Commission, as part of its terms of reference from Government, inquired into the impact of taxation on insurance products.

In his final report, the Royal Commissioner, Justice Owen, made several substantive recommendations on the tax issue in recognition of the important role that affordable insurance plays in the community.

Justice Owen's key recommendations pertaining to insurance tax reform are:-

#### **Recommendation 55**

I recommend that state and territory governments abolish stamp duty on general insurance products. It would be appropriate for this process to be coordinated through the proposed ministerial council with responsibility for general insurance.

#### **Recommendation 56**

I recommend that those states that have not already done so abolish fire services levies on insurers.

#### **Recommendation 57**

I recommend that state and territory governments exclude the cost of the GST for the purposes of calculating stamp duties or any other state or territory levies that are imposed on insurance premiums.

#### **Recommendation 58**

I recommend that governments avoid imposing on insurers levies and other taxes that cannot be passed on to policyholders.

ICA submits that all Australian Governments could be doing more to modernise the tax system as it applies to general insurance and a concerted effort by all governments to implement the Royal Commission tax recommendations would go a long way towards making general insurance more affordable for the community. The maintenance of taxes that penalise those who prudently insure will only continue to discourage people from adequately insuring their assets, placing ongoing strains on government budgets in times of disaster.

## Tax Deductibility Of General Insurance

The taxation of general insurance products could not stand in greater contrast with the Federal Government's treatment of private health insurance.

The private health insurance rebate is 30% of the premium paid to a registered health fund for appropriate private health insurance cover. The rebate is not affected by your level of income.

The rebate can be claimed as:

- A reduction in your private health insurance premium through the health fund or
- A cash or cheque rebate from Medicare or
- A refundable tax offset at the end of the income year through your tax return or
- A combination of all options

While ICA does not oppose the provision of the private health insurance rebate, it does however seem ironic that these tax offsets are offered to persons who insure to guarantee that they receive a certain level of health care when they are ill or suffer some other misfortune causing injury but not to persons who insure, for instance, the family home which is usually their primary asset worth perhaps several hundreds of thousands of dollars.

ICA believes the Commonwealth should consider a wide ranging inquiry into insurance tax reform options. A key issue to be considered by such an inquiry should be the tax deductibility of insurance premiums for home and contents insurance. The adoption of such a proposal would enable those who prudently insure to claim the cost of insuring their principal place of residence as a tax deduction.

Businesses can already claim insurance costs associated with their business as a deduction. The extension of this provision for householders is supported on the grounds of consistency and fairness.

ICA believes that if the Commonwealth considered the tax deductibility of insurance premiums paid by owner occupiers (buildings) and all private residents (contents) to insure a principal place of residence, significant benefits could be accrued by Government and the community.

These benefits include:

- A major financial incentive for householders to insure, thus reducing the incidence of underinsurance and non-insurance.
- A significant reduction in the need for governments to provide ex-gratia payments to support uninsured members of the community who are affected by natural disasters.
- An increased GST take from insurance premiums commensurate with the increased demand for insurance from under insured and non insureds.

ICA recently commissioned Access Economics to further report on these issues and the report is attached at **Appendix C** for the Committee's information.

## **Conclusion and Recommendations**

The natural beauty of Australia's landscape often attracts Australians to 'live among the gum trees' or to at least build their homes at close interface with bushland areas.

In making a decision to live in bushfire prone areas people need to feel confident that in the event of a fire disaster assistance will be speedy and effective. People also want insurance that is not subjected to cascading taxes that artificially boost the cost of premiums – sometimes to prohibitive levels.

As such ICA makes the following recommendations to the Committee:

- 1. That all State and Territories adopt a whole of Government taskforce approach, inclusive of relevant charitable organisations as well as the insurance industry, as part of their State Disaster Plans.**
- 2. That all Australian Governments adopt the recommendations of the HIH Royal Commission with respect to taxation reform; and**
- 3. The Commonwealth conduct a wide ranging inquiry into insurance tax reform options. A key issue to be considered by such an inquiry should be the tax deductibility of insurance premiums for home and contents insurance.**