SUBMISSION NO. 298

Submission to inquiry into residential strata title insurance

I am the resident owner of a strata unit located on the [redacted]. This is an older low-rise block among those along [redacted] being built in the late 1970's. I have been an owner of this property since 2001. I have been a member of the body corporate committee for almost all of that time and Chairman of the committee is recent years.

Having keenly followed this issue for some time there are several aspects on which I wish to comment.

Competition: The Member for Leichhardt has been quite prominent in allegations of 'gouging' by the insurance companies, specifically [redacted]. Predatory pricing is difficult to sustain (and the ACCC would be unlikely to do so) unless it can be shown that there are 'barriers to entry' which have prohibited competition?

As far as I am aware strata title insurance operates almost entirely via insurance brokers, who in turn may have a relationship with the strata body corporate manager for the building. This differentiates it from household insurance where there is more likely to be a direct relationship between the owner and the insurer.

My experience has been that on an annual basis we take the cheapest of three quotes from reputable insurers. The result is entirely price driven with no 'brand loyalty' and may result in frequent changes of insurer which is unlikely to be the case with most house insurance.

The absence of competition has had no adequate explanation and it's also noted that the recent flood insurance report also called for further inquiry combined with a mechanism for temporary intervention integrated with flood insurance proposals.

Market failure: There is clear evidence of 'market failure' within this strata insurance market. This is evident in the failure of increased prices to attract entrants. In fact insurers have withdrawn from the market as prices have been increasing.

There is also evidence of market failure in the disparity between quotations. Only three insurers would provide quotes via our broker for our building last year. The highest quote was more than 100% above the lowest. There is an enormous disparity even between the two lowest bidders of approx. 40%.

For the previous year (2010) the highest of three quotes was more than 40% above the lowest. Either that is a market failure or evidence of extreme variance in risk assessment methodology by insurers?

Commissions: Strata title insurance is generally transacted via insurance brokers on a commission basis. Consequently brokers should be doing quite well from premium increases and have been noted in the media for their justifications of such increases.

However, there is also generally a relationship between the broker and the strata body corporate manager. The current body corporate management agreement for my own block discloses potential commissions up to 20% of base insurance premium.

The most recent AGM documentation for my block discloses in notes a commission of $1,554 paid to the body corporate manager by the broker. This is approx. 12.5% of the total premium. To put this in context the current direct fee paid to the manager is $2,948 ($210 per unit) plus stationery costs etc. Insurance is a critical component and large percentage of the body corporate management business.

These relationships can be obscure, poorly disclosed, and not well known or understood by owners. The relationship between body corporate managers, brokers, insurers and their respective role in the market deserves further attention. Unlike house insurance there are several levels between an owner and insurer.

Qld Strata Title: Strata title legislation can itself create anomalies. Qld strata titles comprise two schedules relevant to owner's costs, a contribution schedule and an entitlements schedule. For most units the entitlements schedule is relevant to insurance costs.

However, the requirements of the relevant Act with regards to allocations for this schedule between units within a building have never been consistently applied by developers, or over time under different Acts. Consequently, insurance costs within a building between different owners may not reflect the intent of the legislation resulting in cross-subsidisation of insurance within a block itself. Again, this may not be transparent to individual owners when they pay fees.

Anomalies in entitlement schedules have previously been a problem for local council rates where this schedule also applies. The Gold Coast and Brisbane councils have previously introduced controversial schemes to correct this, particularly with regard to newer high rise developments, including penthouses, where some had paid very low rates. This situation also extends to locations such as Cairns CBD. However, the primary problem here is with the Queensland Government and failure to address problems of its own legislation.

(Note: Gold Coast Council supplied a report on this to the State Gov't back in 2003 which can be provided)

Body Corporate Budgets: Increases in strata insurance have also been to an extent understated by the imposition of an excess for claims. In my building these have been $10,000 for a named cyclone event and $2,500 for any water damage claim. This means we need to carry at least $10,000 in the sinking fund to compensate which is an additional cost to spread amongst 14 owners.

Another aspect of concern currently is the application of universal OH & S legislation and any potential to increase that component of cover where it applies to body corporates.

Conclusion:

I apologise that this submission has been too rushed on the last day and is not sufficiently explanatory or supported by more detailed information.

Time constraints prohibit further elaboration however I would think it obvious that the above issues do relate directly to the terms of reference. I do have some concerns about the principles the inquiry intends to regard as these seem to avoid responsibility for appropriate design and regulation of a market?

Mark Beath
[redacted]

Terms of Reference

That the House of Representatives Standing Committee on Social Policy and Legal Affairs also inquire into and report on the affordability of residential strata title insurance, particularly in Northern Australia, and factors influencing this, including:

(a) The magnitude of the increases in the cost of residential strata insurance over the past 5 years, the reasons for these increases and whether these increases are likely to be sustained;

(b) The ability of insurers to price risk and the availability of accurate data to allow for this;

(c) The extent to which there is a failure in the insurance market for residential strata properties either generally across Northern Australia or in some regions in particular, for example due to a lack of competition between insurers;

(d) Whether consumer awareness of different insurance options should be enhanced;

(e) The extent to which the nature of body corporate arrangements are contributing to affordability difficulties;

(f) Whether the conclusions regarding (a)-(e) provide justification for government intervention in the residential strata insurance market, noting the existing responsibilities of Commonwealth, state and local governments, for example:

- the Commonwealth Government has responsibility for insurance regulation under the Insurance Act and the Insurance Contracts Act and competition and consumer regulation under the Competition and Consumer Act; and

- state governments (and local governments where appropriate) have responsibility for strata title legislation, building regulation, land use planning regulation and specific state government interventions in insurance markets (for example home builders warranty insurance, compulsory third party insurance).

The Inquiry should have regard to the following principles:

- Individuals and businesses should be encouraged to insure themselves where practicable.
- Government intervention in private insurance markets is justifiable only where, and to the extent that there is clear failure by those private markets to offer appropriate cover.

* Residential strata (or community) titled properties have a body corporate (or owners corporation, strata company, community association or similar arrangement) holding property on behalf of individual owners. The exact legal form varies with state and territory legislation. Bodies corporate are unlimited liability entities, with individual owners having a joint and several, unlimited liability to the body corporate. These properties can take a number of forms, from duplexes to gated communities to small and large apartment buildings. Individuals own a portion of the property (a lot) and there is also common property, of which ownership is shared.