



Half-Day
Seminar

Natural Disaster **Insurance Review** – Discussion of Options

Wednesday, 6 July 2011 • 8.30am – 12.30pm Westin Hotel Sydney

NDIR Issues Paper Actuaries' Response

Daniel Smith

**SMS Questions
0402 293 251**



Actuaries Institute Working Group

- e-mail calling for interested people
- Around 30 people responded
- 15 people have had active involvement
- An Actuaries Institute work in progress – not a specific solution
- Final submission due on the 14th



Structure of Response

- Section 1 – Public Policy
- Section 2 – Response to Issues Paper
- Section 3 – Potential (alternative) models



Section 1 – Public Policy

- Insurance, on its own, does not provide a sustainable long-term solution
- Some properties are not economically sustainable (either due to their position or due to their construction/design)
- A long term goal of risk management and mitigation is required (including relocation)

Section 1 – Public Policy (cont.)

- Cross-subsidisation dulls the price signals that can drive desirable action
- Government subsidies weaken the incentive for individuals (and councils etc.) to take risk mitigation actions
- Intergenerational equity should be considered when assessing mitigation and funding options
- Any funding solution should be transparent and should encourage effective risk management/mitigation



Section 1 – Public Policy (cont.)

- An insurance solution does not address non- and under-insurance, predominantly low income individuals (across all natural perils, not just flood)
- Individuals do not typically assess risk in the same manner as insurers (e.g. 1 in 100 year event)
- Government has an important role to play in assisting individuals who cannot afford access to private insurance



Section 1 – Public Policy (cont.)

- Contents, strata title and small business are important components which need a solution
- Actions of the sea need to be addressed
- National flood mapping is essential. Flood maps need to be widely accessible to all stakeholders



Section 2 – Response to Issues

- There are pro's and con's to any solution. Issues are complex and there is not a perfect solution
- In addition to accessibility and affordability we recommend the assessment of options include:
 - Mitigation incentives
 - Equity
 - Efficiency
 - Practical viability

Section 2 – Response to Issues (cont.)

- The opt-out model does not remove post-inundation debate about whether the damage was caused by flood or storm etc.
- Automatic flood cover poses numerous issues that need to be addressed
 - How will a structure ensure small and medium insurers can compete?
 - How can adverse selection be avoided without compulsion to insure?
 - Could lead to broader “red zoning” and reduced competition for non-flood perils
 - What will APRA’s response be?



Section 2 – Response to Issues (cont.)

- We prefer the engineering threshold to the price threshold
- The use of non-flood premiums as a basis for assessing relative flood risk may cause unintended distortions
- The full economic cost of options needs to be considered, not just the short-term impact – would this make some “expensive” options more attractive?



Section 2 – Response to Issues (cont.)

- Measuring flood risk is complex. Even with detailed flood maps there is considerable uncertainty
- Development of suitable pricing for floods is not cheap. The costs could be prohibitive for some insurers relative to the size of the business
- Consumers are often not well informed purchasers of insurance



Section 3 – Alternative Models

- Market model with subsidies (health insurance)
- Ratepayer funded model for water off the ground losses (central pool)
- Natural disaster pool for declared events
- Event threshold model (non-conditional above threshold and conditional below threshold)
- Variable quota share flood pool
- Compulsory national disaster insurance (base level cover for everyone, private insurance for top up)



Section 3 – Alternative Models (cont.)

- All alternatives have strengths and weaknesses
- Requires measurement against the assessment criteria
- To some extent, the criteria have conflicting interests – some compromise required



Summary of Key Points

- We do not consider that solving the flood insurance issue on its own provides an adequate long term solution
- A long term solution needs to deliver risk mitigation and appropriate cost signals to discourage/prevent inappropriate future developments
- We encourage the Review to consider whether a solution can be developed which improves the level of non- and under-insurance (across all natural perils, not just for flood cover) as well as the impact on low income individuals

Summary of Key Points (cont.)

- We recommend that options be assessed against broader criteria:
 - Accessibility
 - Affordability
 - Equity
 - Efficiency
 - Mitigation incentives
 - Practical viability



Summary of Key Points (cont.)

- We encourage the Review to include contents, strata title and SME's where possible
- We encourage the Review to consider the efficiency of the current system for dealing with funding of natural disasters
- We encourage the Review to consider the impact of actions of the sea (particularly in light of projected rises in sea level)



Summary of Key Points (cont.)

- We support Federal Government sponsored development of Australia-wide flood maps
- We consider that flood maps should be made widely available to all stakeholders (and flood risk well communicated)
- We note the importance of the structure of any pooling arrangement on the behaviours of the participants and puts forward a range of alternative structures



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