



Institute of Actuaries of Australia

**National Disaster Insurance Review Seminar
6 July 2011 Westin Hotel**

SMS Questions with Answers

Q1 a — **John Trowbridge** — Is the Panel looking at options other than a pool to subsidise flood insurance? For example health insurance affordability is addressed through a tax rebate.

NDIR Answer: The Review Panel is keen to have all possible options brought to our attention. We proposed some options in the Issues Paper but they are not the only options.

Q1b – **Gerard Brody** — How did you access that replacement cover would only increase premiums be less than 5 per cent. Would you support it if it hiked premiums by more than 50 per cent?

Gerard Brody - This figure came from the NDIR Issues Paper. I've never seen any evidence that premiums with total replacement cover would increase by 50%. Indeed, there are such policies on the market without such a differential in premium.

Q2a – **John Trowbridge** – You made a comment that some home owners 'should have flood cover but did not'. Why should they? Shouldn't this be consumer choice?

NDIR Answer:

It's not clear the context in which the comment was made. However, at the time that the floods occurred in Queensland and Victoria in January there were a number of factors that affected the ability of households to obtain flood cover:

- not all insurers provided flood cover;
- not all homeowners were aware that their insurance would not or might not cover them for all water damage;
- for some homeowners, accessing flood cover meant a significant price increase compared to the premiums they were used to paying; and
- some homeowners were not aware of their flood risk.

Q2b — **John Trowbridge** — The ability to price/underwrite/offer flood depends on flood mapping. Shouldn't we be discussing the funding for this task? This should be a priority rather than setting pools or forcing insurers to offer cover without ability to assess risk.

NDIR Answer:

The Review Panel agrees that flood mapping is an important issue and devotes a chapter to it in the Issues Paper.

The Issues Paper notes the existence, quality, scope and consistency of flood maps around Australia are variable.

Accordingly, the Panel is seeking views on all aspects of this issue, including on appropriate sources of funding.

Q3a — What comparison has been made on the topic of risk mitigation done by other governments? For example Netherlands mitigation to more than 1 in one thousand. Why is it that our governments do not do risk mitigation to similar levels?

NDIR Answer:

The Review's terms of reference specify that the Panel examine the relationship between mitigation and the availability and affordability of disaster insurance.

The Review has examined a number of other countries' approaches to natural disaster insurance and links to mitigation and a brief summary of them is contained in Appendix 4.

Chapter 19 of the Issues Paper seeks views on lessons that can be learned from international schemes, whether from those featured in the Appendix or from others.

Q3b — It has been suggested that individuals should be encouraged to conduct risk mitigation. The cost of doing this can sometimes be great. Doesn't this just create a new affordability problem?

NDIR Answer:

The issue of who is responsible for undertaking and funding mitigation and the links to insurance is an important element of the review.

Chapter 3 of the Issues Paper discusses moral hazard and risk management and the need to align the interests of all parties — homeowners, councils and insurers.

We are very interested to hear views on how the interests of homeowners, councils, government and insurers can be aligned to allow the parties to work together on mitigation.

Q3c — What are some of the reasons given to date why an engineering approach to determining a high flood risk threshold may be very difficult?

NDIR Answer:

The nature of flood risk and uncertainties around timing, water levels and paths, damage profiles associated with floods, etc cause difficulties for any method.

The need to link affordability with the threshold is a tough task.

Effective data collection and analysis are major tasks, flood mapping is an imprecise matter and information on the nature of individual dwellings may be needed.

An engineering threshold has not yet been designed so its design could well throw up problems not yet recognised.

That said, such an approach may well be feasible and the Review Panel is keen to hear views on how it could be designed.

Q4 a — Given the high cost of living why should Policy holders or rate payers pay more to subsidise 3 per cent of flood prone homes? Or will commonwealth fund pool?

NDIR Answer:

This issue is discussed in Chapter 4 of the Issues Paper and includes an initial consideration of possible funding sources against efficiency, equity and whether it will align the incentives of all stakeholders in order to reduce the risk over time.

The Paper poses a specific question on which parts of the community (some or all taxpayers, ratepayers or policyholders) should ultimately fund the premium discounts and how the subsidies should be allocated.

Q4b — **Gerard Brody** — Who should pay for compulsory flood cover?

Gerard Brody - I'm not advocating for compulsory cover, just that this review provides the opportunity for the costs and benefits of compulsory cover to be considered in-depth. There may be significant benefits that outweigh the costs, much of which would have to be borne by the community generally (i.e. government through taxation).

Q5 — How would access to premium subsidies be means tested? If I have a \$2 million property at Graceville on the Brisbane River should I get a subsidy? Not all flood risk households are low income.

NDIR Answer:

The Issues Paper acknowledged that not all properties located within high-flood risk areas necessarily would receive a subsidy. For example eligibility rules could be built around the considerations of equity, affordability and risk mitigation incentives.

Gerard Brody - There are a range of ways in which benefits are means-tested or concessions are applied.

Q6 — What are the NDIRs views or intentions on researching an affordable price for home building and/or contents insurance as a percentage of net household income?

NDIR Answer:

The Panel is yet to examine this question. If there are approaches to setting an affordable premium that should be considered the Panel would encourage them to be put to us in submissions.

Q7 — Are you concerned with creating an ineffective pool that encourages people to rebuild in high risk areas repeatedly after events at the expense of general tax payers? For example, Texas windstorm association. (sent twice)

NDIR Answer:

Of course. That is part of why we are seeking submissions.

A key guiding principle for the Review is to ensure that all stakeholders face the right incentives.

Q8a — Will the Panel also be considering the issue of a standard flood definition and disclosure — which were part of a separate consultation paper. To me, these issues cannot be completely separated from the NDIR's scope and ideas around automatic flood cover.

NDIR Answer:

The issues of consumer awareness of risk and insurance are specifically addressed by the Review Panel in Chapter 15 of the Issues Paper.

The Review Panel supports the work currently being undertaken on the standard definition of flood and a separate single page key facts statement. The Panel will be taking account of these initiatives in carrying out its work.

Q8b — **Rob Whelan** — If there is no Market failure, why do consumers need to pay thousands of dollars for cover in high flood risk areas?

Gerard Brody - This is a very good question!

Rob Whelan – Product is available in the market; therefore there is no market failure in the classic definition. However the industry has acknowledged that risk premiums will be high (but still available) where the risks are high and has called for government to support those at high risk who can not afford the premium.

Q9 — I'm struggling to understand how a discount system, coupled with transparency around the true cost of the risk will encourage risk mitigation by individuals and councils. Can the review team shed more light on their logic here?

NDIR Answer:

A key issue before the Review is how to align the interests of all stakeholders — households, insurers, and all levels of government — to avoid moral hazard and provide an incentive to mitigate.

The design of any discounts and associated pooling arrangements will be crucial in delivering that outcome. This is discussed in the Issues Paper in Chapter 3 when addressing eligibility for any premium discount and in Chapter 4 that discusses possible funding options.

- For example, an approach in which consumers are explicitly quoted a price reflecting the true cost of their flood risk, separate from their other risks, would convey information that may otherwise not be available on the risk that the consumer faced. That would increase awareness - an important end in itself — and could provide an incentive to reduce the risk.

Q10 — Looking overseas, loss of Government interest once a flood 'solution' has been implemented seems to be a key part of the failure, or partial failure, of these solutions. How can you maintain Government interest over the long term?

NDIR Answer:

The Review is seeking to propose a solution which would align the incentives of all stakeholders. Such a solution should ensure that governments at all levels have an interest in reducing the level of risk faced by the community.

Gerard Brody - Part of the answer here is for stakeholders - consumers, insurers and others - to continue to raise these issues with decision-makers.

Q11 — May a form of national/state catastrophe pool similar to the terrorism pool be the answer? This could be funded via a combination of taxes and council rates. Insurers would retain losses below a certain industry size for example, 1Bn.

NDIR Answer:

We are inviting ideas and would welcome elaboration of this idea if it looks like it could meet the needs.

Gerard Brody - I think this sort of model should be considered as part of the NDIR's analysis.

Q12a – The NDIR TOR says government intervention is only necessary if there is availability AND affordability issues. Availability issues seem to be going away with most insurers offering - so no need for intervention?

Gerard Brody - There are only 54% of home insurance policies that include coverage for flood - I think availability is still an issue. I may be wrong, but I have also heard that it is impossible to get flood cover for some forms of strata-title buildings.

NDIR Answer:

Availability is increasing but, as it increases, the affordability problem becomes more evident.

Q12b — Have ASIC and APRA been engaged on the NDIR proposals? If so what were their views?

NDIR Answer:

In preparing the Issues Paper, the Review Panel consulted widely with key stakeholders, including APRA and ASIC. Their interests naturally revolve around regulatory implications of any proposals.

Q13 — Has consideration been given to proposing an option along similar lines to the NZ earthquake model, where domestic property to a capped sum is insured for flood and actions of the sea?

NDIR Answer:

The Review has examined the New Zealand model as part of its consideration of approaches adopted overseas.

Q14 — **Rob Whelan** — Does ICA see a time in the future when insurers will seek third party recovery action against local governments which continue to authorise new buildings on known flood plains?

Rob Whelan – Recovery action where an authority has been negligent is a possibility in any industry. However, the more likely result in this case is that the properties at risk due to failed local government policy will be uninsurable (affordably) until mitigation action is undertaken.

Q15 — How will governments deal with law suits from property owners when they realise that their property values drop by 30 to 50 percent when flood maps become publicly available?

NDIR Answer:

The Panel notes that a number of councils already do make such information available. For example, the Brisbane City Council's 'Floodwise' program allows the public to access information on flood risk via a publicly available website. We are not aware that making this information available has led to any lawsuits.

Q16a — Shouldn't we be looking to reduce the insurance tax burden to improve affordability not increase it with a big new tax on Australians who aren't flood risks?

NDIR Answer:

The existing tax burden on insurance is important but not central to the work of the Review Panel.

Gerard Brody - Ensuring accessibility and affordability generally, and dealing with the issue of access to insurance in high-flood risk areas, will necessarily involve a trade off.

Q16b **Gerard Brody** - Do you have any thoughts on the NZ experience with insurers and the earthquake commission now locked in high court battle over coverage issues?

Gerard Brody - I'm not an expert on the NZ model, but I do think the model should be considered as part of the NDIR's deliberations.

Q17 — **Insurers on the Panel** — Do the insurers on the Panel agree with Gerard that a move to replacement value insurance will only increase premiums by 5 per cent?

Q18 — From **Peter Cross**, XL Insurance: Has the paper taken into consideration contingent business interruption coverage in the result of a flood pool being implemented if commercial/corporate businesses are included in this pool as a number of current policies in the market place cover such extensions such as prevent of access, supplies/customers in the event of flooding. A large number of claims have risen from the during the QLD floods from these extensions which are often covered with such limits in place. The pool may actually reduce the coverage currently in place.

NDIR Answer:

The Panel is aware that in events such as floods, business interruption insurance can play an important role in the recovery of small business and the community.

The Issues Paper is seeking views on what initiatives could be taken by the insurance industry and the small business community to encourage greater take up and adequacy of business interruption insurance.

Q19 — Flood mapping can never be 100 per cent accurate or complete. How will the pool/rebates deal with properties outside the pool that get flooded? That is what is the process for amending what is or isn't covered by the pool.

NDIR Answer:

The concept explained in the Issues Paper includes the expectation that properties outside the pool would or could be covered by the private market.

Q20 **Rob Whelan** – what proportion of the 85% of accepted Brisbane claims were accepted as riverine flood?

Rob Whelan – Part of the problem with providing a definitive number in response is that different flood definitions have been applied over the entire industry. Meaning that some have been paid as flood, others with the same damage have been paid as water damage. This will be resolved with the standard definition. The points of the 85% is that in the first instance the industry is actually paying a large percentage of the claims, in the second instance it demonstrates that the great majority of policyholders select cover that is relevant to the particular risks they face at their location.

Q21 — Following the NZ EQs parts of Christchurch are declared uninhabitable with government offering buyback. Is that a mitigation alternative to be considered in Australia, very soon? SD, GLA

NDIR Answer:

The Panel understands that some local councils already have home buy-back schemes in place. For example, the Brisbane City Council has been running a voluntary property buy-back scheme since 2005. Such buy-backs, however, make a limited contribution to reducing the flood problems.

Q22 — Given the NFID seems geared towards insurers, how/if does Rob expect it to be used by the public for mitigation purposes? For example, by councils/consumers.

Q23 — If the politicians understand the risks of continuing to allow people to build in flood prone areas, will the NDIR commit to seeking clear and effective political commitment on remedying this issue?

NDIR Answer:

As noted above, the Review is seeking to propose a solution which would align the incentives of all stakeholders.

Q24 — **Gerard Brody** — how did you assess the replacement cover would only increase premiums by 5 per cent? Would you still support it if the impact was 50 per cent?

Gerard Brody - As above.

Q25 — **John Trowbridge** — Does the NDIR expect that land values for existing flood prone properties will decrease, increase or remain the same if they are specifically identified as being flood prone by insurance? How might that impact be managed by government at all levels?

NDIR Answer:

There can be an impact on house prices from both floods and from making information of flood risk available.

Q26a — Rating for full flood cover at an address level will be difficult and expensive as well as risky for insurers, even if they only bear the flood risk for properties outside the high risk zone. What can be done to help them rate flood risk accurately if offering full flood cover is mandatory?

NDIR Answer:

Part of the flood insurance pool concept is that it is the vehicle for assembling and making available, publicly and on a national basis, information on flood risk.

Q26b — Should Councils be required to 'staple' flood risk information to land title documents?

NDIR Answer:

The Panel is supportive of measures to enhance household awareness of flood risk, including by making flood risk information publicly available.

A submission on how such a proposal might work would be welcome.

Gerard Brody - Information about flood risk of particular policies would be helpful for consumers.

Q26c **Rob Whelan** – how many of the high risk 7% will be included in the 80%?

Rob Whelan – This is a fundamental question that we are working on. In the perfect world we need all of the 7% to have purchased flood cover (becoming part of the 80%). Better risk disclosure, competitive options in the market and at an extreme level of risk some form for premium support from those responsible for the mitigation, will all assist in the effort to get as many of the 7% into the 80% who take out flood insurance. It should however, remain their choice to purchase cover or not to.

Q26d **Rob Whelan**; how many insurers will be offering full flood cover to those in high risk properties by 2013?

Rob Whelan - It is expected that all insurers will offer cover at risk rated prices. The 10 most risk prone addresses in NSW right now have a choice of 6 different flood insurance products, each at a different price and with competitive inclusions. This is a free market and insurers (and policyholders) are free to choose products and prices. Removing choice removes competition – in that environment it is unlikely that those at high risk will have any different options to choose from.

Q26e — **Jim Minto**: How would you feel as a life insurer if you were forced to write a new form of life insurance that was difficult expensive and risky to underwrite?

NDIR Answer:

The issues before the Review are longstanding and difficult. We have put forward some options to address them but welcome all views on the implications of the various options we proposed and alternative options that can improve the affordability and availability of flood insurance.

Q27 — In NZ the government bought back properties post EQ. Is that a mitigation alternative here?

NDIR Answer:

As noted above, the Panel understands that the Brisbane City Council has been running a voluntary property buy-back scheme since 2005.

Q28 — What damage to the reputation of the insurance industry has been caused by the Queensland floods? How can this be repaired? Is there mistrust by consumers to the extent that they don't see the point in insuring at all?

Gerard Brody - I would say that the reputational damage to the insurance industry has been significant. An insurance industry that advocates for the status quo is, I think, exacerbating this perception. The research from the Brotherhood of St Laurence with the non-insured did indicate that mistrust of the industry was a factor.

Q29 — Do you think based on the experiences of the US in FAIR (exposure has risen from 40bn to 380bn in 15 yrs) and NFIP having a deficit to treasury of 18bn in 2011 indicates a central pool will just turn one disaster into another?

NDIR Answer:

Careful and effective design of the pool will be crucial to both its financial health and its ability to provide incentives to undertake mitigation.

Q30 a — If the Old Flood Commission of Inquiry delivers a finding that Wivenhoe was not managed as well as it could have by the Old Govt., will insurance companies seek to recoup the claims payouts from the Govt.?

Q30 b — Given the uncertainty of climate change, at what level should land use planning stipulate that new developments be built?

NDIR Answer:

The Review's terms of reference do not extend to us making recommendations on particular land use policies.

Q31 a — What is the NDIRs views or intentions on researching an 'affordable' price for the home building and/or contents insurance as a percentage of net household income?

NDIR Answer:

See response to Question 6.

Q31 b — If the politicians do understand the risks of continuing to allow people to build in flood prone areas, will the NDIR commit to seeking clear, concise and effective political commitment on remedying this issue?

NDIR Answer:

See response to question 23.

Q31 c — **Gerard and John:** Would the community legal and plaintiff lawyers sector prefer that all claims denials, quantum disputes and financial hardship issues are made subject to mandatory referral to the FOS?

NDIR Answer:

The Review Panel has addressed the issue of dispute resolution in Chapter 17 of the Issues Paper. We are interested to hear all views on what can be done to improve internal dispute resolution processes.

Gerard Brody - We would like to see a higher rate of rejected claims being referred to IDR and EDR. The current rates indicate that consumers aren't exercising their rights around dispute resolution - perhaps because they don't know, or they perceive it as difficult, time-intensive and/or not worth it.

Q31 d – **Gerard and John:** We all know that insurees do not generally read PDS document in full. Can it be expected that a reasonable person would read their PDS and KFS within the legislated cooling off period or is this an unreasonable expectation?

Gerard Brody - I think we can all acknowledge that it is an unreasonable expectation for consumers to read their PDS. The key fact sheets have potential to remedy the situation - they should be simple, cover the main aspects of policy including exclusions, and be consumer-tested.

Q31 d — **Gerard and John**: We all know that insurees do not generally read PDS document in full. Can it be expected that a reasonable person would read their PDS and KFS within the legislated cooling off period or is this an unreasonable expectation?

NDIR Answer:

See response to Question 8a.

Q31 e — **John Trowbridge**: Does the NDIR expect that land values for existing flood prone properties will decrease, increase or remain the same if flood prone properties are specifically identified by an insurance mechanism and how might any impact be managed by Governments at all levels?

NDIR Answer:

See response to Question 25.

Q31 f — **John Trowbridge**: You commented that some small businesses might not want to re-expose their business to flood risk, and that may mean people don't want to live in such an area. Is it possible that might be a legitimate outcome or should our default position be that flood prone land is deemed livable in all circumstances?

NDIR Answer:

See response to Question 30 b.

Q31 g — **John Berrill**: Despite KFS, policy terms will continue to drive policy decisions. Can you suggest an alternative contractual model to consumers reading documents which will reduce confusion about coverage?

NDIR Answer:

– See response to question 8a.

Q31 h — **Jim Minto**: If lenders stop lending to flood prone areas, do you think that existing property owners might suffer their loss by a massive drop in the value of their land, instead of massive drops of water?

NDIR Answer:

– See response to Question 25.

Q31 I — **John Trowbridge**: Does the Commonwealth Government have plans in place to create an agency or organization in the nature of a 'Flood Insurance Pool'?

NDIR Answer:

A Flood Insurance Pool was one idea put forward by the Review Panel in the Issues Paper. There are no current Government plans relating to this idea.

Q31 j — Whole towns have been saved from flood by levy banks by Councils who assess and manage that risk. Some towns have no levy banks and they flood.

Mitigation for flood is available and works. Mitigation for cyclones is available and works. Mitigation for bushfires is somewhat available and works to an extent.

Mitigation for earthquakes is somewhat available and somewhat works. It takes effort, care and continuing maintenance by Government.

Q31 k — **John Berrill** — are you suggesting that councils legitimately avoid undertaking flood mapping for fear of being sued? Or should they just meet their legal duties in tort to avoid that concern?

NDIR Answer:

See response to Question 15.

Total 53 Questions