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natural disaster insurance review

the

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Good afternoon.

It is a pleasure to be able to join you today to talk about the Natural Disaster Insurance Review. I’d like to thank the Institute for the opportunity to speak with you.

Over the past few months we have been reminded once again of the devastation that can be wrought by natural disasters. The floods that swept across much of Queensland, the Christchurch earthquakes and the terrible events in Japan all involved tragic loss of life and widespread property destruction.

Natural disasters can also have significant economic impacts. The January 2011 floods and Cyclone Yasi have inflicted extensive damage on public infrastructure and private property alike. Together, they are forecast to reduce Australian economic growth by around half a percentage point this financial year. They will also contribute to inflationary pressures, adding around half of a percentage point to CPI inflation in the March quarter 2011.

They also take a terrible toll on peoples’ lives, so it is vitally important that individuals and businesses be able to rebound from disasters quickly and effectively.

Insurance is an essential component of the recovery because it can limit the financial and economic disruption of such events. For insurance to perform this task effectively it must be there to protect those at risk, in relation to their personal property and their businesses. As we are all well aware, however, there were numerous flood victims who did not have enough cover or who had no cover at all.

While recent events are part of the background to the Natural Disaster Insurance Review, some of you here today will be aware that there are longstanding unresolved issues surrounding insurance for natural disasters. It is these issues that the Review has been asked to look at.

**The Review**

The Assistant Treasurer, Bill Shorten, announced the independent review on 4 March. You can see the media release and the full terms of reference on his website.

I am the Chairman of the Review Panel and my fellow members are John Berrill and Jim Minto. John is a Principal at Maurice Blackburn and has extensive experience in insurance policy wordings and claims and also in consumer affairs. Jim is Managing Director of life insurer Tower Australia and, as well as a long experience in the insurance industry, he has an excellent feel for the connections between suppliers and customers of financial services.

The Panel has been working together now for 5 weeks and is supported by a secretariat established in Treasury.

We are being assisted by the Australian Government Actuary, Peter Martin and have engaged a consultant, Graeme Adams — someone with extensive practical insurance industry knowledge.

You will note that the Review is titled the **Natural Disaster** Insurance Review, not the **Flood Insurance** Review. It will be examining insurance issues for all types of natural disasters — not just floods but also cyclones, earthquakes, hailstorms and bushfires, for both individuals and small business.

**Guiding principles**

The terms of reference include three very specific guiding principles. The first is that government intervention in insurance markets is justifiable only where affordable insurance is not available, i.e. availability and affordability of insurance is a key theme of the Review.

The second principle is that risk mitigation by individuals and governments is a key objective. The context is clear: there need to be incentives on all parties to manage, limit or mitigate their risks. Also it is evident that affordability of insurance is a function of the quality and effectiveness of risk mitigation.

The third principle is that individuals and businesses should be encouraged to insure themselves. As well as the obvious desirability of all those at risk protecting themselves properly, governments and neighbours alike are uncomfortable, even indignant, at seeing governments obliged to give financial support to those who have not made their own arrangements to be protected.

**Progress of the Review**

We only have until the end of September to complete our Review so we will need to maintain momentum throughout.

The Review will be undertaken in four phases – investigation, assessment, policy design and reporting. There will of course be some overlap between the phases but it is important that we focus first on a thorough understanding of the issues before jumping too quickly to policy solutions.

**The Investigation Phase**

The Review team is now heavily involved in the investigation phase. We want to find out what has been the experience of the insured and the insurers. We can then distil the issues and work through them methodically.

Currently we are targeting key stakeholders.

The team is meeting with individual insurers to collect information – both qualitative – on what they underwrite and how, and what has been their experience in dealing with claims - and quantitative — where we are seeking a range of statistics relating to both policies and claims.

We are talking to representatives of consumer organisations to learn about customers’ experiences with insurance. We will also meet with the Financial Ombudsman Service.

We have met with representative bodies, notably the Insurance Council and the Institute.

All have been generous with their time and their information to help us get a clearer picture.

We are also meeting with others that are dealing in one way or another with recent events, for example the Queensland Commission of Inquiry, the Reconstruction Authority and some local councils.

But I stress that this is just the initial phase. Our investigations are aimed not only at understanding the issues ourselves but also at preparing an issues paper, to be released in late May, that will set out the issues as we see them and invite submissions from interested parties.

**Scope of the Review**

The Institute has called for a wide debate. Our terms of reference meet that request.

The Review will examine the extent of, and reasons for, non‑insurance and under-insurance for natural disasters. It is well known that non-insurance and under-insurance exist but their scale and consequences are less well understood.

Secondly, we are to examine the ability of the private insurance market to offer adequate and affordable natural disaster cover for individuals, small businesses and governments. We have been asked to identify any issues that may be impeding the ability of the market to do so, and measures that could be taken to address any impediments.

While the scope of the review includes all natural disasters, we are taking a special interest in flood because of the affordability problem of properties in high flood risk areas.

Thirdly, the Review will examine whether there is a role for the Commonwealth Government in providing disaster insurance or reinsurance to the private sector. We have also been asked to examine the likely impacts of intervention on the private insurance market.

As noted earlier, we are to be guided by the principle that government intervention is justifiable only where there is clear market failure to offer appropriate cover at affordable premiums.

Fourthly, the Review is to examine whether a relationship exists between disaster mitigation measures and the availability and affordability of insurance. There are certainly examples of flood mitigation works undertaken by various levels of government that have reduced the risk of natural disaster. Our task is to consider the extent to which mitigation activities might influence the availability and affordability of insurance.

Finally, we are to consider whether it would be worthwhile to establish a natural disaster fund specifically to support the rebuilding of public infrastructure following a disaster. The Commonwealth currently contributes funds for this purpose under the National Disaster Recovery and Relief Arrangements and the expenditure is currently funded directly from the budget.

Let me stress again that the Review Panel has not yet completed its identification of all the issues raised by our terms of reference, let alone considering solutions.

**Other processes**

The Natural Disaster Insurance Review is one of a number of review processes initiated by the Government. For example, on 13 February 2011, COAG adopted the National Strategy for Disaster Resilience. The Strategy includes steps to improve our understanding of the risks of natural disasters and educating people of these risks. It will also examine ways of reducing the impact of natural disasters through mitigation measures. As part of the strategy, it has been agreed that Heads of Treasuries will report to the National Emergency Management Committee (NEMC) on strategies for maximising the role of insurance in fostering greater community and individual resilience.

Our report will be made available to Heads on Treasuries as part of their deliberations.

This broad, co-ordinated approach to the issue accords with the Institute’s call in February that a solution for flood needs an understanding that the issues are broader than insurance.

Most recently, you may have seen last week that the Assistant Treasurer released two proposals for public comment.

The first is for a standard definition for flood for use in insurance policies. This proposal stems from the confusion and uncertainty that many flood victims felt when trying to identify whether their insurance covered them for riverine flood. The Institute noted in February that ‘defining what ‘flood’ events are covered’ is key to a solution.

The second proposal is for a one page Key Facts statement that summarises the terms of householders’ insurance policies, as a preface to the PDS. This may herald a breakthrough on the design of PDSs for other financial products as well. It is intended to assist consumers to quickly and easily check the basic terms of the policy, including the nature of cover and any key exclusions.

These proposals warrant serious examination by all interested parties including of course the Institute. The closing date for submissions is 13 May

In addition to this initiative,

**Conclusion**

The issues before the Review Panel are not new. For those of you who have experience in the general insurance market, the tracks around natural disaster insurance will be well worn.

We have now been given an opportunity to tackle some of these long-standing issues. We have broad terms of reference that will allow us to fully consider all the relevant issues.

Let me finish by expressing both the interest of the Review Panel and our appreciation of the efforts, the investigations and the level of professional interest that the Institute and many of its members have been taking in matters directly relevant to the Review. In order to address all the issues fully in what is a limited time allowed for the review, we will require the assistance of all stakeholders. So far that assistance has been willingly offered and we are off to a good start. I look forward to ongoing active engagement with the Institute as we work towards finding some answers.

Thank you again for the opportunity to discuss the Review and I look forward to your comments and questions.