

11<sup>th</sup> December 2021

Treasury

By email: [reinsurancepool@treasury.gov.au](mailto:reinsurancepool@treasury.gov.au)

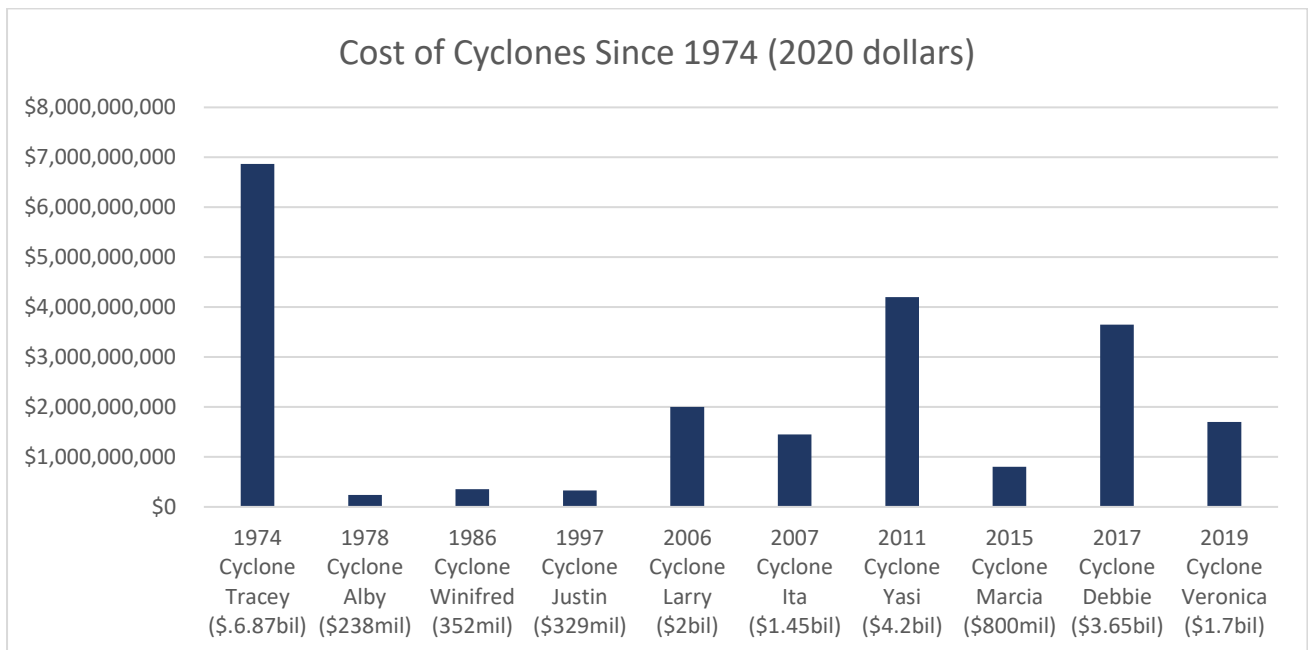
**Re: Response to Reinsurance Pool Draft Legislation**

The Northern Australia Insurance Lobby (“NAIL”) are the voice for consumers on the issue of affordability and availability of insurance in Northern Australia. More information about our organisation can be found on our website [www.nail.org.au](http://www.nail.org.au).

NAIL believes a cyclone and related flood damage reinsurance pool (“the reinsurance pool”) is an effective way to resolve the insurance crisis in Northern Australia. While the draft legislation is a step in the right direction, we believe there are shortfalls in the draft legislation which means it is not fit for purpose. Fortunately, only a small number of changes are needed to make the legislation fit for purpose and we summarise our concerns and recommendations below.

**Eligibility Criteria**

As the reinsurance pool is **cost neutral to the federal government**, the goal of the reinsurance pool should be to ensure it **covers as many in need consumers as possible**, without exposing the Australian Reinsurance Pool Corporation (“ARPC”) to losses above its capacity (i.e. premiums collected and the \$10billion government guarantee). Below outlines insured & non-insured damage sustained by cyclones over \$100mil since 1974 using dollars normalised in 2020.



Source: Wikipedia & RBA Inflation calculator

The historical **data for all losses insured or not**, demonstrates it would be extremely unlikely for APRC to be exposed to insured losses above the \$10billion government guarantee if they covered all damage losses under the reinsurance pool, particularly given building construction regulations have improved significantly since Cyclone Tracey. Therefore, NAIL believes the eligibility criteria should be broader in scope than the proposed legislation.

### Who's Missing?

NAIL believes draft legislation falls short for:

- **Mixed use strata** where commercial use is greater than 20%
- **Commercial buildings** with a sum insured more than \$5million.

### Mixed use strata – Why is this an issue?

Our concerns with the current legislation include:

- **Short-term accommodation** will be considered commercial use. This in essence means many short-term accommodation buildings under a strata title in tourism hotspots will fall through the cracks. **Tourism is fundamental to communities in Northern Australia** and must be adequately covered by the reinsurance pool. Likewise, many people who reside permanently in buildings used for short-term accommodation tend to be older people who retire there for the lifestyle. We know there are strata buildings who are paying as much as twenty times more for insurance for the same building in other parts of Australia, including many buildings on Hamilton Island, Whitsundays, Cairns, Townsville. These buildings will miss out on being eligible for insurance under the proposed legislation.
- The **20% commercial use limit** is very limiting to many buildings and unfairly penalises those who reside in mixed-use strata as their primary residence. Many strata complexes that are marked as commercial (according to the treasury definition) are **owned by mum and dad investors or small businesses**, not big corporations, or Hotel chains. Queensland strata legislation allows that a *“body corporate may adjust the contribution payable by an owner of a lot the proportion of the total risks covered by the policy attributable to activities carried on the owner’s lot”*. We have serious concerns this could have the effect that, for example, in a five lot scheme if one lot is being used for commercial use (more than 20%) that one lot owner could be unreasonably burdened with the difference in premium between a policy insured under the reinsurance pool vs a policy that is not – this could create major disagreements between owners in strata buildings and lead to an increase of disputes in the commissioner’s office.
- While the legislation seeks to provide cover for commercial buildings with a sum insured under \$5million, **commercial strata buildings under \$5million** are not afforded the same access to the reinsurance pool. This means a small strip of shops under a strata title that has a sum insured of say \$2million and houses small businesses will not be afforded cover, while the same commercial building not under a strata title would be afforded cover. This disparity in the legislation is not fair for consumers and will penalise small businesses who own or occupy strata buildings.

### Commercial Buildings – Why is this an issue?

- **Aged care (and other care) facilities** are considered commercial despite the fact they are the primary residence for elderly people and those with other care needs who reside in them. By excluding aged care and other care facilities with a sum insured over \$5million you increase the cost of care for those who reside and use those buildings for residential purposes.
- **Hotels, Motels, Short-term accommodation, Boarding houses with a sum insured over \$5million:** Tourism plays an important part of certain economies in Northern Australia. The reinsurance pool must support accommodation operators and the tourism industry in Northern Australia.
- No context has been provided as to why a **\$5million limit** for commercial buildings has been chosen by the government. NAIL believes this sum insured is too low and will not cover enough consumers, particularly in context that we believe ARPC has capacity to insure larger buildings.

### Recommendations (Eligibility)

NAIL believes the following recommendations related to eligibility should be adopted by Treasury:

- Buildings primarily used for accommodation purposes (including those in strata) should not be considered “commercial use” including but not limited to:
  - o Short Term accommodation
  - o Hotels
  - o Motels
  - o Boarding houses
  - o Aged and other residential care facilities
- Commercial and mixed-use strata buildings should have the same eligibility criteria as other commercial buildings (i.e. currently a limit for \$5million).
- The sum insured limit for commercial use buildings should be higher than \$5million (ideally unlimited, but failing that \$20 million).
- The reinsurance pool should cover mixed-use strata buildings where residential use exceeds 50% (up from 20%);

### The Actual Savings

In Treasury Roundtable discussions held on 6<sup>th</sup> December 2021, representatives from treasury outlined the key mechanisms for savings in the draft legislation:

1. Reinsurance would be offered with **no profit margin** that is taken when insurers reinsure in the private sector; and
2. **The \$10billion government guarantee.**

NAIL has serious concerns about what the actual saving will be for consumers in Northern Australia. Profit margins for the reinsurance sector would be no more than 10%-15% and it is debatable how much the government guarantee would impact the cost of reinsurance.

A saving of less than 20% will have very little impact for consumers paying twenty times more for insurance in Northern Australia. It will fall well short of the 50% saving announced by the Prime Minister when the reinsurance pool was first announced and is far from “parity” that other MP’s have been seeking.

### Recommendations (Savings Mechanisms)

NAIL believes the following recommendations related to eligibility should be adopted by Treasury:

- Treasury should provide more clarity on the proposed pricing and reinsurance premium model adopted by ARPC;
- More savings mechanisms are required to ensure the most in need consumers are at worst saving 50% or at best close to parity with consumers in other parts of Australia. This may include a nominal reinsurance charge to eligible policies that have low/no cyclone risk.

### Review Period

The legislation proposes a review will take place three years after the legislation is passed. It was advised at roundtable meetings that this review date was chosen because the latest date insurers must prescribe to the reinsurance pool was December 2024.

A three-year wait may be too long for some consumers if the legislation is not fit for purpose, particularly if the proposal by Treasury has an adverse effect on availability and affordability of those not covered by the reinsurance pool. An earlier review period is required to ensure that the reinsurance pool meets the needs for consumers even if the review is limited only to eligibility and savings mechanisms.

### Recommendation

NAIL believes the ARPC should conducted review after twelve months limited in scope to consider eligibility and the actual savings, to ensure legislation is meeting the needs of consumers in Northern Australia.

### Conclusion

We believe the legislation in its current form will provide much needed premium relief to a wide number of policy holders in Northern Australia. However, it is our view the draft legislation does not properly meet the needs of consumers in Northern Australia. We believe the **eligibility criteria** and **mechanism for savings** are core issues that need to be reconsidered prior to legislation being passed, otherwise affordability and availability for insurance in Northern Australia will continue to be a “thorn in the side” of the Federal Government.

NAIL believes the seven recommendations provided in this submission will ensure that legislation is fit for purpose when it is released. Thank you for taking time to review our submission.

Kind Regards



**Tyrone Shandiman**  
Chairperson

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