Submission by the
Financial Rights Legal Centre

Northern Australia Insurance Premiums Taskforce

Interim Report, 2015

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About the Financial Rights Legal Centre

The Financial Rights Legal Centre is a community legal centre that specialises in helping consumer's understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the Credit & Debt Hotline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies. Financial Rights took over 25,000 calls for advice or assistance during the 2014/2015 financial year.

Financial Rights also conducts research and collects data from our extensive contact with consumers and the legal consumer protection framework to lobby for changes to law and industry practice for the benefit of consumers. We also provide extensive web-based resources, other education resources, workshops, presentations and media comment.

This submission is an example of how CLCs utilise the expertise gained from their client work and help give voice to their clients' experiences to contribute to improving laws and legal processes and prevent some problems from arising altogether.

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Introduction

The Financial Rights Legal Centre (Financial Rights) welcomes the opportunity to provide comment on the Interim Report of the Northern Australia Insurance Premiums Taskforce. Financial Rights will firstly provide general comments in relation to our approach to considering the options put forward by the Taskforce. Financial Rights will then provide responses to the focus questions posed by the Interim Report.

General Comments

Mitigation, transparency and contestability

Financial Rights believes that the following principles must be central to the development of a final model recommended by the Taskforce to ensure positive outcomes for homeowners and communities, value for money for Australian taxpayers and a healthier insurance market

Firstly mitigation strategies should be encouraged wherever and whenever possible. Any government intervention must be directed to ensuring homeowners and communities in regions affected by cyclones and other extreme weather events mitigate their risks. Be it linking access to any proposed scheme or improving information asymmetries, mitigation should be at the heart and centre of the Taskforce's and government's thinking.

Secondly, premium pricing must be made more transparent. If homeowners and communities are expected to change their behavior with respect to insurance and mitigating risk, it is critical that they be fully informed of the elements that make-up their premiums and any subsequent increases to those premiums. People will change their behavior if they are well informed and appropriately incentivised.

Finally greater contestability needs to be promoted. Homeowners should be empowered to contest decisions made by other parties with respect to their insurance interests including premium pricing and risk assessments and other information provided to and relied upon by insurers and homeowners. Enabling homeowners to challenge for example inappropriate, disproportionate or unjustified premium increases, will improve competition and increase knowledge of the risks and promote mitigation strategies.

The interaction of these three principles should inform the Taskforce's thinking in improving insurance affordability and maintaining sustainable communities in northern Australia and other regions impacted by extreme weather events.

Government intervention should operate nationally

Financial Rights supports the Government's examination of the difficulties faced by northern Australians in acquiring affordable home, contents and strata insurance premiums. Those in northern Australia face uniquely extreme risks by virtue of the climate, environment and geography of northern Australia.

However, it should go without saying that the presence of high frequency natural disaster events is not uniquely limited to this region. The problems faced by those in northern Australia in gaining affordable insurance premiums are also experienced by Australians in other regions of the country where they too faced with a unique set of geographical, environmental and climate-based challenges. While cyclone, storm surges and floods are the key issues in northern Australia, high level flood risk is a significant issue to those in for example, the Hawkesbury-Nepean Valley, the Gold Coast and the Northern Rivers, and extreme bushfire risk remains central to the lives of those in the Victorian Alpine region and the Blue Mountains.

Tables 1 & 2 in the Interim Report[1] detail the affordability of home and contents insurance and proportion of owner-occupiers without insurance demonstrates that NSW and Southern Queensland have particularly high premiums and high levels of non-insurance.

Financial Rights raises this not to diminish the extreme and unique risks faced by those in northern Australia. Rather Financial Rights wishes to ensure that whichever model is finally supported by the Taskforce should be made available to all those Australians in those areas that face extreme risk. Given the constitutional issues raised in the Interim Report, Financial Rights trusts that the Taskforce is aware that a broader, more national approach to the issue may be required.

Climate Change

Financial Rights notes that there is one reference to climate change in the Taskforce's Interim Report stating that "uncertainty about long-term cycles and possible changes in climate make both forecasting cyclone activity in the near term and predicting future cyclone activity very difficult climate." However Financial Rights directs the Taskforce to recent reports from the Climate Council that make it clear that there are "dramatic changes to the climate system happening across the globe" and that "Climate change is increasing the frequency and severity of many extreme weather events" posing "substantial and escalating risks for health, property, infrastructure, agriculture and natural ecosystems."[2]

With respect to cyclones the Climate Council agrees that climate prediction is difficult stating that "the influence of climate change so far on the nature of tropical cyclones themselves is [not] well known, in part due to limited and inconsistent datasets of cyclone behaviour over the past several decades," it does state that "in general, tropical cyclones are projected to become more intense but less frequent."[3]

It is therefore prudent to factor in climate change and the risks this poses for the environment, communities, industry and individual homeowners, when recommending intervention in the

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[1] p. 16, *Northern Australia Insurance Premiums Taskforce, Interim report, 2015*

[2] Climate Council's latest report: "Climate Change 2015: Growing Risks, Critical Choices" By Lesley Hughes And Will Steffen (28/8/15), available at: https://www.climatecouncil.org.au/climate-change-2015-growing-risks-critical-choices

[3] http://www.climatecouncil.org.au/uploads/417d45f46cc04249d55d59be3da6281c.pdf also note p.25 of the "Climate Change 2015: Growing Risks, Critical Choices" By Lesley Hughes And Will Steffen (28/8/15), which states: Tropical cyclones may occur less often but become more intense (medium confidence), and could reach further south (low confidence).

insurance market for high risk regions, particularly with respect to consideration of the length of any intervention.

Indeed, Financial Rights notes that the insurance industry themselves have long factored in the impact of climate change and extreme weather events into their business models and have been arguing for some time for governments to support resilience policies to protect vulnerable communities.

Specific Reponses to Focus Questions

Option 1: A mutual insurer offering cyclone cover to individuals

1. What are the advantages and disadvantages of a cyclone mutual insurer, supported by the Government, with the objective of lowering consumer premiums for home, contents and strata title insurance for people experiencing affordability problems due to cyclone risk? What form of Government support would likely be required?

The key advantage a mutual option has over a government reinsurance pool is that it will be easier to link eligibility for the scheme to mitigation efforts or affordability criteria than it will be to link mitigation under the reinsurance pool option.

It is critical that potential policyholders are encouraged to undertake long-term mitigation strategies to protect their homes from damage. Building this into the structure of the final model recommended will not only protect homes from damage but will reduce premiums and the need for further (or increasing) government intervention over time.

Australian taxpayer money assisting homeowners in high risk regions should be leveraged to ensure long term sustainability of communities. If northern Australian homeowners and communities have not undertaken appropriate mitigation strategies during a period where premiums have been artificially made more affordable, premiums will simply return to the current high levels once that government assistance is withdrawn or tapered off. Indeed Financial Rights believes that without such strategies, homeowners and communities will be worse off given the projected increase in weather event severity.

It is unclear however under the mutual insurer option, how the Taskforce propose to police the necessary reduction of private insurer premiums to reflect the fact that cyclone coverage will no longer be included in their own premiums but will be covered by the mutual insurer.

If insurers do not keep track or communicate the percentage of a homeowner's premium that relates to cyclone risk, how can the Taskforce verify that premiums have been adequately reduced when an insurer is no longer indemnifying that particular risk?

This goes directly to the need for the Taskforce to make further recommendations to ensure transparency and contestability.

A similar issue arose in Victoria when the Fire Services Levy Monitor was created as an independent statutory appointment with substantial powers to protect consumers as Victoria transitioned to a Fire Services Property Levy. The Monitor's functions related only to the insurance-based levy which was abolished on 1 July 2013. The Monitor secured refunds for consumers in excess of $11 million from 56 insurers, who over-collected the Fire Services Levy (FSL) in 2012–13.[4]

Financial Rights details its views and recommendations with respect to contestability and transparency under our response to Policy Contestability, below.

2. How can a cyclone policy be sufficiently defined to fit neatly with a consumer's 'non cyclone' policy purchased from a private insurer so there are no gaps in coverage?

There would need to be a plain language (and consumer tested) standard definition for cyclone damage, cyclonic winds, storm surge and all of the incidental damage that might flow from a cyclone event. A guidance document with recognised scenarios would be helpful for consumers as well as for adjudicators.

3. How should a cyclone mutual insurer price its policies?

Financial Rights again supports the need to ensure that mitigation strategies are encouraged in the design of the final option. Financial Rights therefore suggests that a flat price may not be the optimal form of pricing to meet this end and that a form of pricing that includes a risk component is preferable in order to encourage mitigation strategies. Homeowners should be subsequently made aware of the impact such strategies have on their premium price, necessitating increased pricing transparency.

4. Should insurance from a mutual be open to all or should eligibility be limited, such as to consumers on lower incomes or consumers who take mitigation action?

Financial Rights believes that access to a mutual insurer should be limited to those consumers on lower incomes and/or consumer who have taken or are committed to taking mitigation action. Again it is critical that any intervention encourage consumers to undertake mitigation of risks faced in these regions.

There are strong arguments to support opening up the mutual insurer to all those homeowners within the regions subject to the scheme. The clearest one being that a larger pool will increase funds and possibly promote premium affordability in a way that can be phased out over time. However, providing all consumers access to a mutual has the potential to cause homeowners to 'set and forget' their insurance for the short run, and then have the same affordability problems all over when the scheme finishes.

[4] http://www.firelevymonitor.vic.gov.au/home/

5. What would be required for private insurers to be an agent for a cyclone mutual insurer and sell its policies and manage claims against those policies?

There is the likelihood that consumers will be confused as to who to make a claim against if they have bought a mutual policy as an add-on product to a private insurer's policy. The claims process can be very messy at the best of times but is particularly the case after a natural disaster when homeowners and the community need access to emergency funds quickly and there are large numbers of policyholders seeking information at the same time. If the Taskforce chose to go down this route, consumers would need very clear guidance about who they claim from.

6. What would be a suitable organisational and governance structure for a mutual insurer — a discretionary fund or an APRA regulated entity?

While Financial Rights is relatively agnostic with respect to the appropriate organisational and governance structure of a mutual insurer, it is worth noting that whichever approach chosen the mutual insurer should have a process of internal dispute resolution and access to external dispute resolution. This is the case in NZ with the Earthquake Commission that has internal dispute resolution service, an independent mediation service and access to the NZ Ombudsman. Financial Rights believes however it would be more appropriate that the mutual insurer be a member of the ASIC-approved dispute resolution scheme - the Financial Ombudsman Service Limited - given its expertise with respect to complaints regarding general insurers and insurance brokers.

7. What are the advantages and disadvantages of putting a cap on the payout from the cyclone policy offered by a mutual?

We have no comment.

8. When and how could the Government reduce support for a cyclone mutual insurer?

This is a very tricky question. As detailed above climate forecasts show severe weather events like cyclones may occur less often but become more intense and could reach further south in the coming decades.[5] Beyond the threat of damage from cyclones though the Climate Council states that:

> *Projections for Australia indicate, with considerable confidence, that many extreme weather events will become worse through this century. More frequent and hotter hot days are expected as the century proceeds (very high confidence). Extreme rain events are projected to become more intense (high confidence). Time in drought is projected to increase in southern Australia (high confidence), with a greater frequency of severe droughts (medium confidence).*

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[5] See the Climate Council's latest report: "Climate Change 2015: Growing Risks, Critical Choices" By Lesley Hughes And Will Steffen (28/8/15), available at: https://www.climatecouncil.org.au/climate-change-2015-growing-risks-critical-choices

> *Southern and eastern Australia are projected to experience harsher fire weather (high confidence). … Extreme sea-level events are very likely to increase (high confidence).*

It is therefore not clear that the government will ever be able to step away from assisting those impacted by extreme weather events, be it via preventative market intervention or direct natural disaster funding support.

If the Taskforce does choose a specific date when support for a mutual insurer will cease or be reduced, consumers will need to be informed well ahead of time of the date and what will occur when the intervention ends, particularly the fact that the percentage or level of their premiums will increase at that time. Financial Rights recognises that this might be difficult to estimate, but unless consumers are given warning each year when they renew their insurance they will not be prepared for a significant increase in premiums. Repeated warnings may help encourage long-term mitigation strategies, or even an exodus of some home owners out of high risk regions who recognise that they will not be able to afford insurance once the scheme has been phased out.

Option 2: A reinsurance pool for cyclone risk

9. What are the advantages and disadvantages of a cyclone reinsurance pool, supported by the Government, with the objective of lowering consumer premiums for home, contents and strata title insurance for people experiencing affordability problems due to cyclone risk? What form of Government support would likely be required?

The advantages that a cyclone reinsurance pool has over a mutual insurer is that the claims process for consumers would be easier than with a cyclone mutual insurer. Consumers would have a policy with a single insurer that covers all of their risk, and regardless of which insurable event occurs they would deal directly with their one insurer.

Furthermore, the reinsurer option also seems at least on the surface to be the least disruptive to the current insurance market.

However, there are a number of disadvantages to the reinsurer option.

The first is that it would be very hard to tie mitigation action to eligibility for the scheme without further intervention. Bringing insurance premiums down by reducing reinsurance costs will be a welcome salve for already financially stretched consumers who are put off by high premiums. However cheaper and more accessible insurance will not by itself encourage homeowner or community mitigation strategies nor will it discourage continued development in high risk regions. If the aim of the scheme is to simply lower costs rather than encourage changed behaviour then the reinsurer option seems fit for purpose. Financial Rights is of the view that the Taskforce need to aim higher and promote longer term positive outcomes for the community and for Australian taxpayers.

But even the lowering of prices is not 100 per cent guaranteed. Private reinsurers may not reduce the rates that they charge to insurers if they do not believe the Australian cyclone reinsurance pool will effectively cover all the risk that cyclones pose to homeowners. The reinsurance pool option as currently detailed also relies solely on market competition for insurers to reduce their premiums even if reinsurance rates are lowered. As has been detailed by the Taskforce there is currently very little competition in the northern Australian market and no guarantee that this will increase with the presence of a reinsurance pool.

Finally it is Financial Rights' strong view that without improved transparency and contestability there is very little guarantee of appropriate decreases in premium prices.

10. How should a cyclone reinsurance pool be designed to best fit with insurance companies' existing arrangements, including reinsurance arrangements? For example, how could cyclone and cyclone damage be defined so as provide certainty about what is covered by the reinsurance pool?

We have no comment.

11. How should the price insurers pay for reinsurance from a reinsurance pool be calculated?

We have no comment.

12. What are the advantages and disadvantages of limiting payouts available under a reinsurance pool arrangement?

We have no comment.

13. When and how could the Government reduce support to the market through a cyclone reinsurance pool?

As discussed above, it is not clear that the government will ever be able to step away from assisting those impacted by extreme weather events, be it via market intervention or direct natural disaster funding support.

However if the Government does choose a specific date when support for a cyclone reinsurance pool will reduce, consumers need to be regularly informed of date, what will occur when the intervention ends and the percentage that their premiums will increase at that time. Repeated warnings may help encourage long-term mitigation strategies, or even encourage some home owners to move away from high risk regions should they recognise that they will not be able to afford insurance once the Government has reduced its funding.

14. How could a cyclone reinsurance pool scheme be structured to provide an incentive to policy holders to mitigate the risk of cyclone damage?

As detailed above there is nothing inherent in the concept of a reinsurance pool that will encourage mitigation strategies. Financial Rights suggests that a carrot and stick approach may be necessary. For example, consumers that do not undertake mitigation strategies may have to pay a levy which helps fund the pool. While consumers on low incomes, or consumers that are unable to self-mitigate for some verifiable reason would be exempt from the levy, those homeowners that are able to undertake mitigation strategies would have to do so within a certain time period or pay the levy to the pool. Other strategies are detailed under the Mitigation section.

Other options

15. Are there any other approaches that could lower premiums in areas where affordability is a concern due to cyclone risk?

Taxes and duties

Financial Rights supports reducing taxes and duties on insurance. Taxes certainly add to affordability concerns, especially in a time when premiums are rising. Having the Commonwealth Government subsidise the states for the 20 per cent lost revenue in insurance tax might be a more effective way to lower insurance premiums than either of the market intervention options. One would expect a 20 per cent drop in premiums at the very least whereas neither the mutual insurer option nor the reinsurance pool can guarantee insurers will reduce premiums by any set amount. Again increased transparency and contestability will be required to ensure that these savings are passed on.

Direct Subsidy

Financial Rights only supports a direct subsidy to consumers if eligibility for that subsidy is somehow tied to mitigation activities. Insurance costs are a clear signal to consumers about the level of risk their home is subject to. If the Government interrupts this risk signal, there will be no incentive for consumers to mitigate, or move elsewhere and the same affordability concerns will still exist when subsidies are phased out. Government should concentrate intervention on supporting mitigation costs, addressing information asymmetries or significant information gaps and supporting better regulation of the insurance market to promote significantly increased transparency and contestability.

Policy contestability and disclosure

Financial Rights believes that there are significant problems with respect to policy contestability and disclosure that need to be addressed across the industry. However these issues have a particularly negative impact on those regions impacted by cyclones and extreme weather events given the fact that there are fewer options available for people to gain insurance.

Currently, the main way premiums or insurers' decisions in relation to offering insurance is "reviewed" is by consumers shopping around to see what other insurers are offering, a mechanism next to useless in northern Australia.

Outside of market forces the only other mechanism available is for an insured to make a request in writing under section 75 of the Insurance Contracts Act 1986. An insured however can only use section 75 when either their insurance is cancelled or by reason of some special risk relating to the insured or to the subject-matter of the contract, or when the insurer offers insurance cover to the insured on terms that are less advantageous to the insured than the terms that the insurer would otherwise offer.

However, the Act and section 75 provide no guidance as to what information the insurer is obliged to provide in its written reasons, and there is no mechanism for review in the event the decision of the insurer is erroneous or based on incorrect information.

In insurance markets with limited suppliers such as Northern Australia, competition is not an adequate mechanism for consumers to 'review' insurance premiums. If all insurers are using incorrect data or not taking into account localised factors, then competition fails.

As a possible alternative, a consumer may make an application to the Financial Ombudsman Service (FOS). However FOS has a very limited decision making power when it comes to reviewing premiums. The FOS Terms of Reference provides:

> *Clause 5.1 - The service may not consider a dispute:*
>
> *b) about the level of a fee,* ***premium****, charge or interest rate – unless:*
>
> *(i) the Dispute concerns non-disclosure, misrepresentation or incorrect application of the fee, premium, charge or interest rate by the Financial Services Provider having regard to any scale or practices generally applied by that Financial Services Provider or agreed with that Applicant; …*
>
> *e) in the case of a Dispute about a General Insurance Policy – about rating factors and weightings the insurer applies to determine the insured's or proposed insured's base premium which is commercially sensitive information;*
>
> *f) about a decision to refuse to provide insurance cover except where:*
>
> *(i) the Dispute is that the decision was made indiscriminately, maliciously or on the basis of incorrect information; or*
>
> *(ii) the Dispute pertains to medical indemnity insurance cover; …*

In the 2013/14 financial year 38 consumers lodged disputes about insurance cover refusals (under clause 5.1(f)) and were excluded from FOS, and 19 consumers lodged disputes about premiums and weightings and had the dispute refused (see the 2013/14 FOS Annual Report on page 49). The Annual Report does not indicate whether FOS accepted any disputes made by consumers under the above sections.

A review of all of the decisions made by FOS to date shows that 15 determinations have been issued in their jurisdiction about "incorrect premiums", the majority of decisions relate to consumers being misled.

Significantly, determination number 218234 recognises that an insurer has the commercial decision to increase premiums, but must disclose the basis of the increase beyond providing a general explanation. In Financial Rights' view, this was a good decision of FOS as it enabled a consumer some degree of contestability of an unexplained premium increase when the consumer's personal circumstances (and risk assessment had not changed) and the insurer could not justify the increase in the cost. However, this represents one decision of FOS and has not resulted in any insurers giving reasons on renewals as to increases in insurance costs.

It is Financial Rights' view that insurers should not be able to hide behind vague reasons and unsubstantiated assertions about how premiums are priced. They should have to substantiate premium pricing across all forms of insurance. In the home and contents space it is essential.

The failure of industry to have any mechanism of review of the accuracy of premium calculations is of significant detriment to consumers. This failure also provides no guarantee that any household mitigation strategies or idiosyncratic household conditions are taken into account when determining premiums. Consequently, premium prices cannot be said to be "accurate" signalling of risk as there is no contestability or transparency in their calculation.

A consumer may reject the premium as an inaccurate reflection of their risk, and where there are few insurers in the market place (or they are all relying on the same incorrect information) a consumer may decide to self-insure or be forced to be uninsured not only for the risk of the hazard but for all claims (where they cannot get any level of cover).

If a robust dispute mechanism was in place creating greater transparency and contestability of premium pricing, Financial Rights expects the following benefits to arise:

a) consumers may be persuaded they are at risk, and decide to incur the cost to insure;
b) consumers may undertake personal mitigation strategies; or
c) consumers may lobby local government for local mitigation strategies.

In the absence of this information, consumers are in the dark and may be making poor decisions. If they could have a premium pricing decision reviewed by an independent body, consumers may be more likely to believe the risk assessments on their properties.

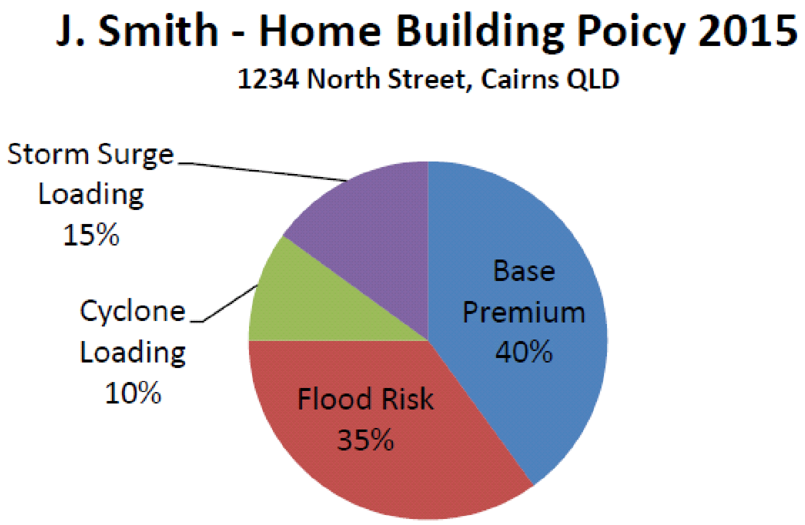
Financial Rights strongly supports all the suggestions detailed by the Taskforce including reforms that will:

- require insurers to provide an explanation to policyholders where there has been a significant change in premiums or non renewal of the policy;

- change the Terms of Reference of the Financial Services Ombudsman so that it can hear disputes about the level of premiums if there has been an unfavourable change to an insurance policy and adequate reasons have not been provided to the policyholder; and

- require insurers to provide disclosure on the individual components that make up the overall cost of the premium.

With respect to this final point it is Financial Rights firmly held view that insurers be required to provide information as to the component pricing in insurance. Knowing what makes up the price of a premium will better inform consumers about risk and what effect mitigation strategies may have on reducing insurance premiums or what behaviours or conditions might increase premiums. Component pricing information should apply uniformly across all insurers but will be particularly helpful in addressing a lot of the issues faced by those in northern Australia and other regions hit by extreme weather events. It would provide an easy to read, easy to understand signal to consumers of the risk factors taken into account when premiums are set. For example:



The above would communicate to a consumer the risk, and the potential benefits of changing behaviour to mitigate that risk. To assist homeowners even further, information could be provided directly below the chart detailing practical tips on how a homeowner could mitigate cyclone risk and lower their premiums.

Financial Rights recognises that such a proposal may face objections from some in the insurance industry on the basis that pricing information is "commercially sensitive". Even if "commercial sensitivity" is accepted to be an issue, Financial Rights does not believe that it is insurmountable and asserts that there are simple and creative ways to ensure such information is sufficiently obscured without denying homeowners the right to basic information about their insurance. For example, the component pricing could use percentage figures that are heavily rounded up or even display information using graphics and images only. The number of solutions available is in our opinion limited only by the will of vested interests rather than anything unique about insurance as a product. It is Financial Rights' view that "commercial sensitivity" must no longer be used as an excuse to continue to keep homeowners in the dark about an essential and important product and should not be wielded as some sort of trump card to prevent any and all changes aimed at improving information asymmetry in the insurance market.

Financial Rights also supports greater access to information on natural hazard mapping, modelling, exposure and risk. Insurance companies are not currently required to make this information available to consumers even when it applies directly to their premium price. This information should be made available by the government through a clearinghouse website (or any alternative government supported measure) to ensure data consistency and reliability. There should also be a review mechanism built in to the process. Financial Rights remains concerned that the Insurance Council of Australia 's Building Resilience Rating Tool may not be accurate, be difficult to contest if it doesn't take into account individual mitigation and resilience factors, and will not guarantee that premiums accurately match the ratings provided.

In addition to these ideas, Financial Rights also supports insurers printing on a renewal notice the policyholder's premium that they paid the previous year in order to more effectively inform consumers of price rises in their premiums. Insurers should also explain why the price has increased. Such an idea was recommended by the Victorian Government's Fire Service Levey Monitor, is currently being investigated by the UK's Financial Conduct Authority and is being introduced by international insurer AXA. The Consumer Action Law Centre is also a strong advocate for this proposal.[6] This however would need to be mandatory for all insurers as encouraging a voluntary disclosure of this sort would encounter problems from those insurers (especially smaller insurers) wishing to avoid being the first to move.

Recommendations

The Financial Rights Legal Centre recommends the following approaches to promote pricing contestability, disclosure and transparency:

a) Amend s 75 of the *Insurance Contracts Act 1984* requiring insurers to provide written reasons for why premiums were increased on request in writing from a policy holder. These reasons should include any increased risk factor that the insurer has become aware of.

b) Alternatively, if legislative change is not feasible, the General Insurance Code of Practice should be amended to include a requirement for the insurer's IDR team to provide reasons for significant premium increases after a request in writing by the policy holder.

c) Change FOS Terms of Reference to allow disputes about the level of a premium if there has been an unfavourable change to an insurance policy (or if the insured has recently undertaken mitigation strategies on their home which have not resulted in a reasonable reduction of premiums) and the insurer's IDR response has failed to include adequate reasons for the change.

d) Require insurers to provide component pricing of premiums.

e) Require insurers to provide the prior year's premium price on renewal notices.

[6] http://consumeraction.org.au/insurance-companies-prove-your-loyalty-to-us-be-upfront-on-price-rises/

Mitigation

16. What can be done to encourage greater efforts to mitigate the risk of damage from cyclones? Are there impediments to insurance premiums being responsive to mitigation action by property owners?

Providing consumers with more information about risk and mitigation strategies is an important first step. For example, this interim report discusses two mitigation issues which we as consumer advocates do not believe consumers are necessarily aware:

Firstly, the Interim Report explains how building codes are designed to reduce injury to people, but not necessarily mitigate against any structural damage in a cyclone.[7] This information should be clearly and simply communicated to consumers. Homeowners who have gone to great lengths to make sure their homes are up to the latest building codes may be under the impression that their insurance will be reduced accordingly, when in fact they have not reduced their risk of cyclone damage at all.

Secondly the Interim Report explains that steps can be taken to reduce the vulnerability of cyclone damage before a storm hits which are pretty minor.[8] Things like removing loose items around a property or undertaking small-scale home improvements. This information should be distributed to homeowners, and tenants on a regular basis. Many residents in cyclone areas might be new to the area and not aware of the small steps they can take to greatly reduce their cyclone damage risk.

Homeowners will only be incentivised to undertake mitigation projects on their own properties if there is a corresponding reduction in premiums. There does however seem to be some impediments to insurance premiums being responsive to mitigation action. The first is that insurers might want verification of the efficacy of a mitigation strategy before reducing premiums. This could be resolved by having post-mitigation premiums be subject to some independent review. Currently there is no independent or regulatory mechanism for homeowners to contest post-mitigation premiums. Financial Rights supports the Interim Report's discussion of an independent inspection process to determine the vulnerability of a property to cyclone damage, give information to consumers about what mitigation action they might take, and provide verification of all mitigation action that a property owner has undertaken. If an insurer refuses to recognise mitigation strategies undertaken by a homeowner by lowering premium, or does not lower premiums enough there must be a way for that homeowner to lodge an independent dispute.

We believe consumers will be more likely to take up adequate insurance and undertake mitigation strategies if they can identify a correlating reduction in premium. This however can only be done by promoting great transparency and contestability, as outlined above. Consumers can and do recognise some personal and property risk, but the current premium pricing system does not provide any reliable benefits to homeowners to take any personal mitigation strategies.

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[7] p. 12, *Northern Australia Insurance Premiums Taskforce, Interim report, 2015*
[8] p. 14, *Northern Australia Insurance Premiums Taskforce, Interim report, 2015*

17. What are the advantages and disadvantages of establishing an independent assessment process to determine the vulnerability of a house to cyclone damage and to verify what mitigation work has been undertaken? How could such a process be established?

Financial Rights supports the development of an independent assessment process. The biggest advantage of establishing an independent assessment process is that it will give insurers the verification they need to reduce premiums, which will in turn incentivise mitigation action by homeowners. Again, homeowners will only be incentivised to undertake mitigation projects on their own properties if there is some certainty around a corresponding reduction in insurance premiums.

Consumers respond very positively to independent assessment and review mechanisms. Consumers will not always trust an insurer to give them an honest answer about their risk or the corresponding cost of indemnification. An independent process is often seen as much more reliable.

The disadvantage of a scheme like this is that it would cost money. Would it be industry funded, Government funded, or funded by homeowners that want to use it? If the answer is the latter, this will not help with affordability issues, and it is not much different from a homeowner paying for a builder to come assess their property. Financial Rights recommends that an independent assessment process be at least partially funded by industry or the Government.

18. What are the advantages and disadvantages of (a) establishing a rating system for building vulnerability to cyclone damage that could be publicly disclosed at the time of sale, and (b) establishing a centralised database on building information that could be accessed by insurers?

In principle, Financial Rights supports a rating system for building vulnerability and a centralised database. Financial Rights recommends that information be distributed to households by governments and insurers through council rates notices, rental contracts or insurance renewal statements. Financial Rights is especially supportive of providing this information through council rates notices since that would help eliminate any suspicion that a homeowner might have regarding hazard information being provided directly through private insurance companies.

However Financial Rights does have concerns about the contestability of an established rating system. If this rating system or database (once it is made available to the public) does provide accurate and independent information about household vulnerability, it will be a very useful tool for homeowners in assessing their own risk. Unfortunately, there is currently no evidence that such a tool will eventuate or meet any intended objectives. Financial Rights is concerned that household data may not be accurate, and will be difficult to contest if it does not take into account individual mitigation and resilience factors of households. Financial Rights is also concerned that even if the ratings are accurate, this will not ensure that insurance premiums will accurately match the ratings.

Again it is critical that a holistic approach be taken to ensure that mitigation strategies are encouraged, transparency and disclosure be promoted and contestability be built in to any final proposal from the Taskforce.

It is simply not enough to lower consumer premiums in cyclone and other extreme weather event areas to promote mitigation strategies. It is unrealistic to think that lowering premiums "may release some funds for the property owner to take steps to reduce the vulnerability of their property to cyclone damage."[9] Most consumers will simply take the savings and use the money for other household and living expenses. This is particularly the case for those on lower incomes. Expecting homeowners and communities to take action during the period of government assistance is similarly unrealistic without explicit incentives and significant improvements to premium transparency and regular communication and information

19. What are the advantages and disadvantages of using increased excesses or policy exclusions to reduce the number of small claims following a cyclone?

Increasing the size of an excess for making a claim in the event of a named cyclone is not a bad idea for reducing premiums. However this would need to be clearly disclosed to homeowners, and insurers would need to be more transparent about what component of the premiums are based on cyclone risk in order to lower the overall premium accordingly.

Recommendation

The Financial Rights Legal Centre supports:

a) the development of an independent inspection process to determine the vulnerability of a property to cyclone damage and other extreme weather events;

b) an independent assessment process at least partially funded by industry or Government;

c) greater provision of mitigation information to homeowners in regions subject to cyclones and extreme weather events.

[9] p. 44, *Northern Australia Insurance Premiums Taskforce, Interim report, 2015*

Concluding Remarks

Thank you again for the opportunity to comment. If you have any questions or concerns regarding this submission please do not hesitate to contact the Financial Rights Legal Centre on (02) 9212 4216.

Kind Regards,

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