



**NATIONAL INSURANCE BROKERS ASSOCIATION OF AUSTRALIA (NIBA)
SUBMISSION ON INQUIRY INTO RESIDENTIAL STRATA TITLE INSURANCE**

16 January 2012

ABOUT NIBA

NIBA is the voice of the insurance broking industry in Australia. NIBA represents 500 member firms and over 2000 individual qualified practising insurance brokers (QPIBS) throughout Australia. Brokers handle almost 90% of the commercial insurance transacted in Australia, and play a major role in insurance distribution, handling an estimated \$16 billion in premiums annually and placing around half of Australia's total insurance business. NIBA member firms also place large and special risks into the world insurance markets.

Over a number of years NIBA has been a driving force for change in the Australian insurance broking industry. It has supported financial services reforms, encouraged higher educational standards for insurance brokers and introduced a strong independently administered and monitored code of practice for members. The 500 member firms all hold an Australian financial services (AFS) licence under the Corporations Act that enables them to deal in or advise on Risk Insurance products.

ABOUT INSURANCE BROKERS

The role of insurance brokers

The traditional role of insurance brokers is to:

- Assist customers to assess and manage their risks, and provide advice on what insurance is appropriate for the customer's needs;
- assist customers to arrange and acquire insurance; and
- assist the customer in relation to any claim that may be made by them under the insurance.

In doing the above the insurance broker acts on behalf of the customer as its agent. Insurance brokers offer many benefits to consumers:

- assistance with selecting and arranging appropriate, tailored insurance policies and packages
- detailed technical expertise including knowledge of prices, terms and conditions, benefits and pitfalls of the wide range of insurance policies on the market
- assistance in interpreting, arranging and completing insurance documentation
- experience in predicting, managing and reducing risks



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- assistance with claims and a higher success rate with settlements (about 10 per cent higher than claims made without a broker).
- in limited cases insurance brokers may act as agent of the insurer not the insured but where such a relationship exists the customer is clearly advised up front.

EXECUTIVE SUMMARY

NIBA is pleased to be able to make a submission to the House of Representatives Standing Committee on Social Policy and Legal Affairs inquiry into the affordability of residential strata title insurance.

NIBA has already made submissions to the Committee's inquiry into the operation of the insurance industry following recent natural disaster events and to the Natural Disaster Insurance Review, and many of the issues raised in those submissions have relevance here.

The issues are complex. NIBA supports the principles behind the inquiry, being that:

- Individuals and businesses should be encouraged to insure themselves where practicable; and
- Government intervention in private insurance markets is justifiable only where, and to the extent that there is clear failure by those private markets to offer appropriate cover.

In relation to the current inquiry, NIBA respectfully submits that a further core principle is the desirability for strata corporations, given their unique nature, to effect and maintain comprehensive insurance coverage in respect of potential damage to the corporation's property, and in respect of public liability and related exposures. This provides protection to individual lot owners in the case of serious damage to the property, and to third parties who may sustain injuries arising from negligent conduct on the property.

NIBA's submission can be summarised as follows:

- While the market for strata title insurance is now experiencing difficulties, NIBA does not believe that there is any evidence of a broad market failure with the issues being specific to limited locations and narrow range of risks.
- NIBA is aware there has been a significant increase in price and reduction in capacity of strata insurance, principally in Queensland and Western Australia above the 26th parallel, given the unique nature of the risk profile of such areas and recent adverse claims experience.



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- Anecdotal information being provided to NIBA suggests insurance for these risks has traditionally not reflected the true cost of the risk that was transferred to insurers, and the recent cyclones and storms have resulted in insurers and reinsurers carefully re-assessing their experience and reviewing the terms and prices on which they are prepared to offer cover in these areas.
- In the absence of serious market failure for this type of insurance, there is no justification for Government intervention in the operation of the insurance market. However, NIBA suggests steps might be taken to ensure transparency of claims information to inform and facilitate responsible and reasonable underwriting and pricing decisions by insurers and reinsurers.
- In the meantime, strata corporations should be encouraged to retain the services of Qualified Practising Insurance Brokers to assist them with the placing of their insurance cover.
- Finally, all levels of Government should continue to implement the COAG objectives of promoting resilience in the community, given the likely repetition of serious weather events in Northern Australia, and north Queensland in particular, in the future.

NIBA sets out its response to the terms of reference below but also notes that feedback is still being received from members and if any significant additional issue is identified, NIBA will pass this on to the inquiry.

BACKGROUND ON STRATA INSURANCE

Strata insurance meeting certain minimum criteria is required by the relevant State and Territory legislation in every jurisdiction to varying degrees. Typically it covers property damage to body corporate assets and common property (in QLD see for example [section 178 of the Body Corporate and Community Management \(Standard Module\) Regulation 2008.](#)) and public liability for common property and relevant assets (in QLD see for example [Section 187 of the Body Corporate and Community Management\(Standard module Regulation 2008\).](#)

The mandatory insurance requirement arises because of the moral hazard associated with the potentially unlimited liability of each lot owner to the entity. If a building suffers an uninsured loss, each owner would be jointly and severally liable, irrespective of their role in relation to the insurance.

Strata insurance can combine other covers and can include features such as directors and officers insurance for the members of the owner corporation's governing board or committee.



The type, availability and cost of strata insurance (as with other insurance) varies greatly according to the location and type of the risk. In this regard, it is important to bear in mind that residential strata title properties could be as small as a simple duplex residential building comprising two lots, or could be large multi storey buildings with hundreds of lot owners including, on occasion, some degree of commercial activity. Strata title has also been adopted for multi-lot properties spread across an area (horizontal strata title), in addition to multi story buildings (vertical strata title).

Strata managers, given their close relationship with the entity, often play a large role in sourcing the insurance. Insurance brokers play a role as well, especially for those entities that realise the significance and importance of appropriate advice in relation to such insurance.

The main difference is that insurance brokers will typically be authorised under their Australian financial services licence to provide personal advice on what insurance is appropriate for the needs of the body corporate. Insurance brokers are professionally qualified to assist clients with the identification and management of risks, and the purchase of appropriate insurance in what can be a difficult and complex market.

Strata managers will typically not be authorised to provide such advice and will usually source the insurance from one or a limited number of insurers only.

NIBA RESPONSE ON TERMS OF REFERENCE

THE MAGNITUDE OF THE INCREASES IN THE COST OF RESIDENTIAL STRATA INSURANCE OVER THE PAST 5 YEARS, THE REASONS FOR THESE INCREASES AND WHETHER THESE INCREASES ARE LIKELY TO BE SUSTAINED

Feedback from members has been that pricing has changed significantly with increases starting in 2010 and continuing to increase in 2011 and 2012. In some cases members have seen examples of very substantial increases in the northern regions. NIBA is also aware that some insurers have ceased to write strata title insurance in Northern Australia.

The reasons behind the increases will be better answered by the insurers concerned. However, we understand it is likely to be as a result of a number of factors, such as:

- specific portfolio exposures of the relevant insurers (e.g an insurer may seek to reduce any imbalance in a portfolio top heavy in north Australian risks);



- adverse claims experience, especially in the north above the 26th parallel. Insurers have advised that poor recent aggregate claims experience had suggested that many strata risks had been under-priced for some time. The significant weather related risk exposure of the North is not generally seen as an issue with the Southern States;
- the types of risk concerned:
 - the type of building can make a significant difference with the older the building, the more difficult and costly it is to insure.
 - The lack of appropriate mitigation measures implemented by State and local government, especially in the Northern areas. e.g poor building standards and allowing for development in flood prone areas.
- reinsurer concern relating to natural disaster risks in this area of the world (e.g . Brisbane floods, Cyclone Yasi, Japan's tsunami and New Zealand's earthquakes) causing the global reinsurance market to substantially increase prices and/or reduce exposure to the Asia/Pacific region.

Members have advised that the recent imposition of substantial cyclone excesses on policies do not appear to have significantly altered insurers' approach to the risk.

Members have also indicated that they felt the insurance market has been under priced in previous years, but that pricing may have now gone to the other extreme. NIBA is of the view that sound underwriting practices combined with strategies to promote the resilience of the communities affected should ultimately lead to a more stable and reasonably priced insurance market.

NIBA is happy to work with the inquiry further in obtaining or considering further information provided by insurers if necessary.

THE ABILITY OF INSURERS TO PRICE RISK AND THE AVAILABILITY OF ACCURATE DATA TO ALLOW FOR THIS

Sound insurance underwriting requires access to and analysis of comprehensive data on the recent and long term claims experience of the risks concerned. This includes data relating to claims arising out of the insurer's own portfolio of business, and data relating to the broad industry claims experience in the relevant area.

Whether current data is sufficient for insurers to price the risks appropriately is a question more appropriately addressed to insurers and underwriters. However, in order to encourage an informed and competitive market, including the opportunity for new entrants to offer products in this sector



of the market, NIBA would support any measures to collect and publish relevant industry data relating to these types of risks.

Insurance underwriting also involves some element of subjectivity, with the underwriter determining the weighting to be given to each variable. The recent significant increases in premium may suggest that this subjective element has been overly pessimistic, but NIBA does not have access to data on which a considered view could be formed.

There is no doubt, however, that the insurance industry in Australia has had to bear very significant claims costs as a result of numerous severe weather related events across the country in the past 18 months. The financial results of a number of insurers confirm the extent of the insurance losses incurred in Australia in recent times.

NIBA does note that rises in insurance costs are relatively widespread e.g tropical residential and commercial property markets and home insurance, although lack of capacity is less of an issue for areas other than strata title insurance.

NIBA is happy to work with the inquiry further in obtaining or considering further information provided by insurers if necessary.

THE EXTENT TO WHICH THERE IS A FAILURE IN THE INSURANCE MARKET FOR RESIDENTIAL STRATA PROPERTIES EITHER GENERALLY ACROSS NORTHERN AUSTRALIA OR IN SOME REGIONS IN PARTICULAR, FOR EXAMPLE DUE TO A LACK OF COMPETITION BETWEEN INSURERS

Members have identified to NIBA that their main concern is the lack of Residential Strata Insurers in the market place and recent large decreases in capacity, especially for risks in Northern Australia. There is not a total market failure at the present time, but where cover is available it is now much more expensive than in previous years.

This mainly affects Queensland and Western Australia. Whilst in Western Australia mining companies manage the risk themselves there is a growing number of entities that are affected. In the Northern Territory the feedback is that the strata insurance arrangements of the Territory Insurance office, whilst expensive relative to southern States, is generally more competitive than insurance offered in north Queensland and northern WA.

NIBA understands that the largest specialist strata insurer does not write cover in the north and existing participants generally have small market shares at the national level.

Members have indicated that the lack of capacity is likely to be as a result of:

- some insurers withdrawing from the market due to adverse claims experience; and



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- others limiting their exposures to higher risk geographical areas, potentially as a result of reinsurance arrangements and treaty renewals.

Whilst NIBA has not formed a view, it is worth considering whether a lack of competition could to some degree be contributed to by the fact that strata managers act as a conduit in organising strata insurance. Such managers would typically have a relationship with one or a limited number of insurers. Unlike a traditional insurance broker they would not provide personal advice on the most appropriate strata insurance available for the strata body corporate.

Strata managers are also likely to have only limited knowledge of the insurance process, the terms and conditions of policies available in the market place, and the range of insurers offering cover in this area. NIBA strongly supports any moves to encourage owners corporations to seek professional advice and assistance on risks and insurance matters from a Qualified Practising Insurance Broker.

WHETHER CONSUMER AWARENESS OF DIFFERENT INSURANCE OPTIONS SHOULD BE ENHANCED

NIBA is strongly of the view that insureds are best served by utilising the services of a Qualified Practising Insurance Broker, who can provide personal advice on their risks and their insurance needs and options.

NIBA expects that most body corporates simply rely on the strata manager to obtain quotes from one or a limited number of insurers and do not seek advice or guidance on the appropriateness of the cover for their needs. In many cases, significant cost savings and increases in cover can be obtained by using the services of an insurance broker.

In addition, in the case of a claim being made, the services of an insurance broker in representing the client in relation to the claim can be of great value in ensuring the quick and appropriate resolution of the claim.

An appropriate notice provided by strata managers of the importance of such advice services may make the availability of such services more obvious and ultimately benefit the entity.

THE EXTENT TO WHICH THE NATURE OF BODY CORPORATE ARRANGEMENTS ARE CONTRIBUTING TO AFFORDABILITY DIFFICULTIES

NIBA has not received any feedback from its members that the nature of the body corporate arrangements is contributing to the affordability difficulties.



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WHETHER THE CONCLUSIONS REGARDING THE ABOVE PROVIDE JUSTIFICATION FOR GOVERNMENT INTERVENTION IN THE RESIDENTIAL STRATA INSURANCE MARKET, NOTING THE EXISTING RESPONSIBILITIES OF COMMONWEALTH, STATE AND LOCAL GOVERNMENTS, FOR EXAMPLE:

- **THE COMMONWEALTH GOVERNMENT HAS RESPONSIBILITY FOR INSURANCE REGULATION UNDER THE INSURANCE ACT AND THE INSURANCE CONTRACTS ACT AND COMPETITION AND CONSUMER REGULATION UNDER THE COMPETITION AND CONSUMER ACT; AND**
- **STATE GOVERNMENTS (AND LOCAL GOVERNMENTS WHERE APPROPRIATE) HAVE RESPONSIBILITY FOR STRATA TITLE LEGISLATION, BUILDING REGULATION, LAND USE PLANNING REGULATION AND SPECIFIC STATE GOVERNMENT INTERVENTIONS IN INSURANCE MARKETS (FOR EXAMPLE HOME BUILDERS WARRANTY INSURANCE, COMPULSORY THIRD PARTY INSURANCE).**

NIBA does not believe that there is any evidence of a broad market failure with the issues being specific to limited locations and narrow range of risks. On this basis, NIBA does not believe there is sufficient justification for Government intervention in this area of the insurance market.

However, NIBA suggests that in order to ensure the market is operating at its optimum, any available steps should be taken to ensure transparency of claims information, in order to inform and facilitate responsible and reasonable underwriting and pricing decisions by insurers and reinsurers.

NIBA does note, however, the very heavy exposure of Australian insurers to claims arising from severe weather events in the past 18 months. The price of insurance is ultimately a reflection of the cost of claims, and with increasing claims costs in recent years, it is virtually inevitable that prices will increase as a result.

As noted in NIBA's previous submission on flood, all levels of government share a level of responsibility as:

- local government have approved high-density development in high risk locations and State-level policies and planning frameworks have encouraged these kinds of developments. NIBA understands that the Western Australian Government is actively promoting and supporting a high density development via its Pilbara Cities program.
- lack of appropriate risk mitigation programs or data at local, State and Federal levels that help define or reduce relevant risk and allow for better underwriting.



The imposition of taxes on insurance by the Commonwealth through GST collections and the States through stamp duties significantly increase the cost of insurance in Australia. NIBA has opposed such taxes for many years and consideration should be given to what relief may be provided in this respect for taxes on strata insurance.

Like the Council of Australian Governments (COAG) NIBA is of the view that there is a need for “a whole-of-nation resilience-based approach to disaster management, which recognises that a national, coordinated and cooperative effort is needed to enhance Australia’s capacity to prepare for, withstand and recover from disasters.”

The solution must involve a true combination of:

- Federal/State Government/local council initiatives; and
- private sector and consumer initiatives, including insurance cover.

There is no doubt there will be further extreme weather events across Australia, and particularly in the northern regions. The need is greater than ever for Government promotion of highly resilient communities, clear and appropriate land use planning and controls, sound building standards, effective flood management and mitigation, and minimisation of likely harm and potential loss. It is only if these all occur that insurance will be able to be provided at reasonable cost to policyholders.

Another crucial component is to promote the value of obtaining personal advice provided by Australian Financial Services Licensees such as Qualified Practising Insurance Brokers. There is no substitute for the provision of advice from professionally qualified advisers such as insurance brokers in obtaining competitively priced and appropriate insurance or proactive management of an insurance claim.

Despite Government attempts to simplify insurance documentation (which have continued since the introduction of the financial services reform legislation), the reality is that an insurance product is by its very nature of some complexity and consumers will not generally be inclined/or well equipped to read/understand them. The services of a professional adviser can go a long way to reducing insurance related issues.

If you would like to discuss any aspect of this matter further do not hesitate to contact us.

Dallas Booth
Chief Executive Officer
National Insurance Brokers Association of Australia

