



Allianz Australia Insurance Limited

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Ms Marion Scrymgour MP
Chair
Joint Select Committee on Northern Australia
PO Box 6100
Parliament House
Canberra ACT 2600

By email: northernaustralia.joint@aph.gov.au

Dear Chair

Inquiry into the Operation and Implementation of the Cyclone Reinsurance Pool

Allianz Australia (Allianz) appreciates the opportunity to make this submission to the Inquiry into the operation and implementation of the Cyclone Reinsurance Pool (the **Inquiry**). Allianz was supportive of the policy decision to establish the Cyclone Reinsurance Pool (the **CRP**), and has worked with the Treasury and the Australian Reinsurance Pool Corporation (**ARPC**) over the past year to settle the legislative and operational framework underpinning the CRP. Allianz remains of the view that, appropriately designed, a reinsurance facility in conjunction with measures to enhance the resilience of properties to extreme weather events, is the most efficient and effective way of addressing affordability of insurance in regions exposed to cyclone and/or flood risk.

Allianz anticipates that the CRP will deliver reduced premiums to customers, particularly customers in regions with a high cyclone risk. Allianz has an accelerated program of work underway to operationalise participation in the CRP and plans to transition our householder portfolio (home building, contents and landlords) into the CRP by 1 January 2023. This will be followed by other eligible classes (i.e. residential strata and small business property insurance) during 2023. Customers are not required to take any action to benefit from Allianz's participation in the CRP. During 2023, Allianz also expects to look at options to grow market share in Northern Queensland and Western Australia, which will inject greater competition into these markets.

Our submission briefly outlines the rationale for introducing the CRP and the anticipated impacts it is likely to have on Allianz customers. In making this submission, Allianz provides general information on the likely impact of the CRP at the portfolio level to assist the Committee, noting that individual customer impacts will depend on a customer's circumstances, including the location and risk profile of their property.

1. Insurance affordability and cyclone and flood risk

For many years, Allianz has been of the view that there is a growing problem with the affordability of property insurance for some residential homeowners and small businesses vulnerable to cyclones and floods.

The higher cost of home insurance in Northern Australia reflects the risks associated with the extreme weather perils facing the area, particularly the vulnerability to cyclones. Insurance

premiums for properties exposed to cyclone risk can be very expensive. In some circumstances, a Northern Queensland property can face premiums many times that of a similar property not vulnerable to cyclone risk, particularly, if the property:

- was built before 1982, when higher cyclone building standards were introduced;
- is constructed of weatherboard, rather than brick;
- has had recent claims and is, for example, ineligible for no claims discounts;
- is located on low lying land close to the coast and is thus also vulnerable to storm surge, which is often caused by cyclones or extreme low pressure storm events that cross the coast; and/or
- is located on the side or top of a hill (where windshear can result in wind speeds nearly twice that impacting adjoining lower areas).

Allianz has also been concerned about the affordability of property insurance for consumers and small businesses subject to the risk of flood. The annual premium of a home building and contents policy for a modest property (i.e. a total sum insured of \$400,000) with a high flood risk can exceed \$20,000. Homeowners with both high cyclone and/or flood risks can face premiums of more than twenty times those of other Australians.

At such extreme levels, premiums cease to act as an appropriate price signal and drive other behaviours and decisions which have a range of negative consequences. Some of these include non-insurance, intentional underinsurance, disincentives to invest in residential property, discouraging population growth in whole regions and, resulting, lower overall levels of economic activity.

Allianz therefore has been supportive of a government-subsidised reinsurance facility to assist with lowering premiums for customers exposed to extreme cyclone and/or flooding risk. Allianz notes that the CRP is designed to be revenue neutral to the government over the long term and, hence, is not designed as a mechanism to provide a government subsidy to address affordability. Allianz notes that the revenue neutrality constraint will limit the CRP's ability to reduce premiums to all customers experiencing affordability challenges. Allianz also notes that the CRP's coverage of only cyclone-related flooding means that it will not have any impact on the affordability of insurance for those with high flood risks in southern areas of Australia, for example, those located in Northern NSW and North/West Sydney impacted by the record-breaking February/March 2022 floods or those located in Western NSW, Victoria or Northern Tasmania impacted by the October 2022 floods. Allianz remains concerned about the affordability of flood insurance for property owners who won't benefit from the CRP as currently designed.

The CRP, while likely to be effective in reducing premiums for some customers in the short to medium term, should be complemented by comprehensive measures to help mitigate against, and adapt to, the risk of cyclones and flooding. The cost of home insurance is directly related to the risk of loss faced by a property and in many cases, the cost and frequency of that loss comes down to how well the property is protected from the effects of damaging natural weather events. Mitigation, adaptation, land use planning, development controls and robust building standards are all critical in ensuring that all Australians have access to affordable property insurance.

2. Introducing the CRP

The *Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Act 2022* (the Act) establishes the CRP and requires insurers, for eligible policies, to purchase reinsurance from the ARPC. The objective of the CRP is to enable insurers to purchase reinsurance cover at a lower rate from the ARPC (which operates on a non-profit basis) than would otherwise be possible through the commercial reinsurance market, the cost savings of which is intended to reduce premiums paid by end-customers most exposed to cyclone and related flooding risk.

Although operating nationally, the Act in practice requires insurers underwriting home building and contents, small business property and residential strata policies to purchase reinsurance cover from the ARPC for policies with a cyclone and related flooding risk exposure; all such eligible policies are required to be ceded to the CRP by 31 December 2023. For policies captured by the CRP, the ARPC will provide reinsurance cover which responds to:

- loss or damage in relation to cyclone and related flood claims, including wind, rain, rainwater, rainwater run-off, storm surge, and riverine flood damage caused by a cyclone; and
- claims for cyclone and related flood damage arising during a cyclone event, which lasts from the time a cyclone begins until 48 hours after the cyclone ends.

Other perils (e.g. non-cyclone related storm damage and flooding) and loss outside of the 48 hour window will not be covered by the CRP and will continue to be covered by insurers' reinsurance arrangements with commercial reinsurers. In preparing to join the CRP, a substantial amount of work is required to ensure the various reinsurance arrangements in place between Allianz, the ARPC and our commercial reinsurer work effectively and seamlessly in providing comprehensive reinsurance cover.

Under the CRP, the ARPC charges reinsurance premiums to insurers according to a defined premium formula at an individual policy level, taking into account the cyclone risk of the property being insured. The ARPC's premium formula has taken into consideration the intent for the CRP to be revenue neutral to government over the longer term.

Given Allianz proposes to transition its householder portfolio into the CRP well before the deadline, our analysis on the potential impact of the CRP on this portfolio is well advanced. Based on the reinsurance premium rates published by the ARPC on 1 October 2022, our analysis indicates that average premiums to be offered to existing customers exposed to cyclone and related flooding risk will be around 6 percent lower than premiums that would have been offered had Allianz not transitioned to the pool, comparable with modelling conducted by the ARPC¹. The reduction in premiums resulting from the CRP itself will be more impactful for regions² highly exposed to cyclone and related flooding risk, with average impact of around 9 percent in Northern Australia and up to 30 percent (on average) in some regions within Northern Australia.

This initial analysis is provided to the Committee to assist in considering the likely impact of the CRP. Allianz notes that average regional premium reductions mask a wide range of impacts from the CRP for individual customers, with the CRP having only a modest impact for customers with a low to moderate exposure to cyclone and related flooding risk. Allianz expects that the CRP will result in no changes for customers with no exposure to cyclone risk.

¹ Finity (2022), *Cyclone Reinsurance Pool – Premium determination applying from 1 October 2022*, report to Australian Reinsurance Pool Corporation, 28 September 2022.

² References to 'regions' are to geographical locations as defined by the CRESTA (Catastrophe Risk Evaluation and Standardising Target Accumulations) Zones used as the industry benchmark in managing natural hazard risk.

- 4 -

Within regions, premium impacts will vary depending on individual property risk characteristics, which means the reductions resulting from the CRP will be greater than 30% for some customers. In particular, in line with the intent and design of the CRP, customers experiencing the greatest affordability pressures will generally benefit most. Allianz notes though that the high frequency of extreme weather events over recent years and other claims cost inflation factors (e.g. building materials) are resulting in larger than usual increases in property premiums nationally. The final premium charged to customers will be the net effect of the CRP-induced reductions and general premium rises. For example, for customers with only a moderate cyclone risk and no related flooding risk, the impact of the CRP may only result in moderation of a premium increase, rather than a premium reduction.

Allianz, however, is of the view that the CRP will help achieve the objective of providing premium relief to households most vulnerable to cyclone and related flooding risk. Allianz expects that the quantum of achieved premium relief will be reviewed over time as the CRP becomes fully operational. Allianz looks forward to continuing to work with government in finetuning the CRP as required to ensure the quantum of premium reductions delivered meets community expectations.

We trust this submission is of assistance to the Committee and look forward to engaging with the Committee further in its inquiry.

Yours sincerely

James Fitzpatrick
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