

RACQ Insurance Submission:

Northern Australia Insurance Inquiry

ACCC Issues Paper
21 December 2017

BACKGROUND

RACQ Insurance (RACQI) is pleased to provide this submission in response to the Australian Competition and Consumer Commission Northern Australia Insurance Inquiry Issues Paper, dated 24 October 2017.

RACQI was established in 1971 and is wholly owned by The Royal Automobile Club of Queensland (RACQ) which was established in 1905 and is owned by more than 1.6 million members as a mutual organisation. It has a strong Queensland focus to its business, providing insurance cover to over 1.4 million individual policyholders throughout Queensland and northern New South Wales.

RACQI has an intimate understanding of the affordability pressures and challenges facing homeowners and the industry as a whole when it comes to the pricing of risk in Queensland, especially northern Queensland. RACQI advocates that the full range of factors be taken into consideration in calculating home building and home contents insurance premiums and that market conditions, underlying risk factors and underwriting considerations have ultimately driven premium prices. RACQ focuses its business primarily in the Home, Contents and Motor spaces and the comments in this submission reflect that focus.

This submission is a simple illustration of the commitment RACQI has to support the exploration of alternatives to provide some relief to this pressure felt by homeowners.

The submission is geographically focused on the northern Queensland region, in line with RACQI's geographic boundaries; however the key considerations covered in the response are expandable to other regions that are subject to high natural peril risk.

1. COSTS, PREMIUMS AND PROFITS

The sophistication and granularity of risk assessment and insurance premium rating has increased markedly in recent years as insurers such as RACQI have sought to gain a better understanding of the drivers and profiles of risk.

Despite this, there has been persistent dialogue suggesting that insurers price household risk at postcode level in North Queensland. While this may be the case for some, RACQI operates a highly sophisticated pricing engine which allows natural peril risk such as flood and cyclone to be priced at property address level.

This approach not only allows for the accurate assessment of risk with all contributing factors taken into consideration, it also ensures that the consumer is paying a premium that is accurate and commensurate with the risk posed by their individual property. One outcome of this enhanced accuracy is that the pricing spread between different risks has grown, reducing the cross-subsidisation of poorer risks by homeowners in less risky areas.

As highlighted, RACQI has developed the capability to price household insurance at the individual property level. RACQI operates a highly sophisticated pricing engine which allows this granularity in pricing natural peril risk, with all individual factors of risk being considered in the calculation. While the application of this approach resulted in dramatic premium increases to certain high risk sectors of the community which were previously 'subsidised' by other, lower risk premiums, other sectors of the community were not impacted by premium increases, while some premiums decreased.

In 2012, RACQI implemented compulsory flood cover for all household insurance policies across Queensland. This implementation was supported by the ability to price at property address level and according to the actual risk. While this did result in an increase in premiums for some property owners, the increase was reflective of the risk that those properties posed, and simply highlights that the historical premiums charged in the region were not commensurate with, or reflective of, the risk faced.

In addition to developments in flood risk pricing, RACQI also further developed pricing capability for other natural perils. Of particular relevance in northern Queensland is the capability to determine cyclone risk at an individual property address and provide a premium that accurately reflects the risk faced by the individual property. As with flood, this has had varying impacts on premiums for policyholders, and is reflective of the risk of each property.

The peril modelling sophistication provides a prospective view of risk that forms the foundation for pricing, and is not reflective of a burning cost ratio view, which could drive short-termism and unreasonably high premiums.

In considering costs to the consumer, it is also essential to consider the reinsurance costs incurred by insurers such as RACQI, which are reflective of the exposures to risks in areas prone to natural disasters, particularly where investment in mitigation infrastructure is lacking. Reinsurance pricing is hardening globally in the face of extreme natural peril losses recently experienced.

2. COMPETITIVENESS OF MARKETS

RACQI, unlike some market competitors, continues to provide insurance cover to the whole of Queensland, and does not impose any generic new business embargoes on home insurance policy sales.

RACQI acknowledges that high risk zones such as northern Queensland are difficult to insure, however our position is underpinned by our focus on implementing real benefits for the consumer.

RACQI distributes its products directly through owned channels such as branches and our own branded website, as well as in a very limited way, through some agencies.

It is important to note that in deciding to compete in a high-risk area like northern Queensland, different insurers' varying appetite for risk, which includes capital requirement considerations as well as commercial decision making and strategic alignment, must be considered. In areas without investment in mitigation frameworks (such as infrastructure investment, retro-fitting to building codes etc) deciding to enter such a market may not be palatable for those organisations.

3. CONSUMERS' EXPERIENCE WITH INSURANCE

3.1 Choosing insurance

RACQI provides an individually risk rated price along with a quality product and established claims management practices.

3.2 Finding information

RACQI invests significantly in continuously developing the communication methods and content to enhance the clarity provided across all our channels. Despite this, and more generally than northern Queensland, it is observable that there are widely varying degrees of education and understanding of insurance principles and products and how they work across the community.

3.3 Switching

RACQI does not have comment to offer on this aspect.

3.4 Affordability

RACQI currently provides customers across Queensland with various voluntary excess options, and actively supports this approach to increase affordability.

RACQI also provides a Pay By The Month (PBTM) option for premium payments, which is a small monthly fee. Other market competitors structure their PBTM option as a percentage of the underlying premium, which penalises consumers who already have a high premium by further compounding the issue.

In addition, RACQI was the first to offer a cyclone mitigation discount of up to 20% of the premium, depending upon the mitigation work that has been undertaken on a given property.

4. MITIGATION

Mitigation is the foundation of any and all efforts to reduce insurance premiums on a sustainable basis, as this will reduce the risk of damage and claims following an event, rather than simply transferring the cost of the risk.

This was recognised in the final report of the Northern Australia Insurance Premiums Taskforce, wherein a number of potential options were considered. The resultant recommendations promote both individual household efforts towards mitigation as well as Government investment in incentive schemes, subsidisation for household mitigation, research into better building mitigation options and public infrastructure works. RACQ notes the Hon Kelly O'Dwyer's media release of 18 December 2017 accepting the finding of the Taskforce that mitigation activities are the only way to reduce premiums on a sustainable basis.

There appears to be a degree of willingness of North Queensland homeowners to take measures to cyclone proof their home if it resulted in a reduced premium. RACQI recognises this willingness and as noted above, was first to market in 2016 with a cyclone mitigation discount that offers a premium reduction of up to 20%, depending upon the range of mitigation activities undertaken on the property.

It should be noted that most of home buildings with particularly high premiums are not believed to be compliant with the cyclone building code based on their year of construction.

5. REGULATION

The role played by taxes and duties on insurance premiums should be acknowledged, as these can add up to 20% on top of the actual risk premium being charged. RACQI advocates the reduction of taxes and duties on insurance premiums for areas of high risk, potentially targeted to demographics experiencing home insurance affordability issues. The approach provides an effective and simple premium reduction mechanism. Incentives such as this could also be easily linked to mitigation activities to ultimately reduce the risk faced by the consumer.

Application of this approach also provides added flexibility for the Government, as it is not restricted specifically to cyclone risks and can be considered for other high-risk areas, e.g. bushfire or flood, should insurance affordability become an issue. While there would be a small loss of revenue associated with tax and duty reductions, this would provide consumer relief for those experiencing affordability stress.

SUMMARY

As a Queensland based insurer owned by a mutual, RACQI measures all business decisions and actions by how they could potentially impact RACQ Members and consumers in the wider market. RACQI fully supports seeking relief for the affordability pressures felt by a segment of homeowners in northern Queensland.

RACQI notes the number of investigations and explorations of insurance affordability and competition in Northern Queensland undertaken over the last number of years and sees that investment in mitigation of risk is the key to affordability rather than additional inquiries.