AUSTRALIAN COMPETITION & CONSUMER COMMISSION

Insurance monitoring

Second report following the introduction of a cyclone and cyclone-related flood damage reinsurance pool

December 2023

Acknowledgment of Country

The ACCC acknowledges the traditional owners and custodians of Country throughout Australia and recognises their continuing connection to the land, sea and community. We pay our respects to them and their cultures; and to their Elders past, present and future.

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Land of the Ngunnawal people
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Executive summary

The damage to private property caused by extreme weather events, including cyclones, can be severe. It can lead to the displacement of people from their homes, disruption to business activity and lasting damage to communities.[1] Due to the greater risk of cyclones in northern Australia, insurance premiums are significantly more expensive compared to other parts of the country, leading to cover becoming less accessible and affordable in these regions. A changing climate, which is expected to exacerbate extreme weather events in the future, has heightened concerns about access to affordable insurance.

In 2022, the Australian Government established the cyclone reinsurance pool (the pool) to help lower premiums for households and small businesses with high cyclone risk by reducing the cost of reinsurance. The government directed the ACCC to collect data over 5 years to monitor the impact of the pool, assess whether savings from the pool are being passed through to policyholders, and see whether the pool is delivering on its intended outcomes. We will observe the impact of the pool as it develops over the full 5-year monitoring period.

This is our second annual monitoring report.

In this report, we have extended our analysis of insurers' prices, costs and profits. We continue to find that policyholders in northern Australia are paying, on average, substantially more for their home insurance compared to the rest of Australia. Insurance prices in northern Australia remain high and increased in 2022–23, but by less than in the rest of Australia.

Consumers across northern Australia urgently want access to more affordable insurance. Through our engagement with communities this year, we continued to hear about the financial pressures that consumers and small businesses are facing to obtain the insurance they need and their high hopes for the savings that the pool may deliver.

A key objective of the pool is to make insurance premiums more affordable, but the pool is still in transition. Insurers only began to join the pool at the start of 2023, and most that have joined did so around or after July 2023. This timing means that the early effects of the pool are unlikely to have extended to most consumers yet, or be directly reflected in this year's data reported to the ACCC, which is from the 2022–23 financial year. Large insurers are required to join the pool by 31 December 2023 and small insurers by 31 December 2024.

We note that damage to property from tropical cyclones in 2022–23 was relatively limited, although other extreme weather events have had an ongoing impact on communities around the country.

In this report, we have also sought to understand how insurers are implementing the pool and their approaches to passing on any savings it generates. We have observed that implementing the pool in accordance with the government's policy intent is complicated. Many insurers have been required to change their reinsurance arrangements as well as their approaches as to how they have traditionally modelled and priced risk.

The way that insurers are choosing to approach the pass-through of any savings to consumers, both as they implement the pool in the short term and as they adapt their systems over the longer term, may directly impact the effectiveness of the pool in achieving savings for consumers at high cyclone risk. Similarly, individual insurers' capability and determination to reward consumers for private risk mitigation investments will also influence the extent of savings the pool will generate for consumers.

1 Explanatory Memorandum – *Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Bill 2022* [1.3]–[1.4].

The combination of these and other factors can result in very different outcomes for policyholders depending on their location and their insurer. Furthermore, the combination of insurers entering the pool at different times, the time required for insurers to fully implement pricing changes, and differing policy renewal cycles mean that consumers may not see the full impact of the pool on their premiums for quite some time.

In addition to providing the government with an important evidence base as to how the pool is working, the ACCC continues to engage with a range of concurrent initiatives examining related insurance market concerns. Our 2017–2020 Northern Australia Insurance Inquiry was a wide-ranging investigation into the availability and affordability of home, contents and strata insurance. We consider that many of the findings and recommendations made in the final report of that inquiry remain relevant today.

Prices remain much higher in northern Australia, although prices in the rest of Australia increased by more

Home, strata and small business insurance products in northern Australia form a relatively small share of the national insurance market, accounting for around 8% of gross earned premium in recent years. Within northern Australia, the majority of gross premium is earned in north Queensland, although this has decreased slightly from 81% in 2019–20, to 77% in 2022–23.

Home, strata and small business insurance premiums remained much more expensive in northern Australia in 2022–23 compared to the rest of Australia (see Table ES.1 for a summary of key price findings). However home and strata insurance premiums in the rest of Australia increased by more in the past year, which may reflect the impact of significant disasters in southern parts of the country in 2022. We did not observe any significant widespread price effects from the pool given the limited insurer entry in that financial year. As we monitor developments over time, we expect to observe the impact of the pool on premiums emerge gradually and for any savings to be passed on to consumers.

The average premium in 2022–23 for a combined home and contents policy was most expensive in north Western Australia ($4,395, a slight decrease of 3% in real terms compared to 2021–22), followed by the Northern Territory ($2,922, an increase of 6%) and north Queensland (remained steady at $2,918). The rest of Australia experienced an increase in average premiums of 7%, with policyholders paying on average $1,779 in 2022–23.

In nominal terms (that is, without adjusting for inflation), premium increases were more significant. It is useful to observe nominal changes as this is how consumers will typically read and experience their renewal invoice, and compare how their premium has changed from year to year. Between 2021–22 and 2022–23, the increase in nominal terms was most pronounced in the rest of Australia (15%) but the northern regions still experienced continued growth in premiums: the Northern Territory (13%), north Queensland (7%) and north Western Australia (4%).

Even when measured on a per $100,000 sum insured basis, average annual premiums were still significantly higher in north Western Australia ($716), but now followed by north Queensland ($518) and then the Northern Territory ($385). The rest of Australia was cheapest at $252, or around one–third of the cost faced by policyholders in north Western Australia and half that faced by policyholders in north Queensland.

Table ES.1: Premiums in northern Australian regions and rest of Australia

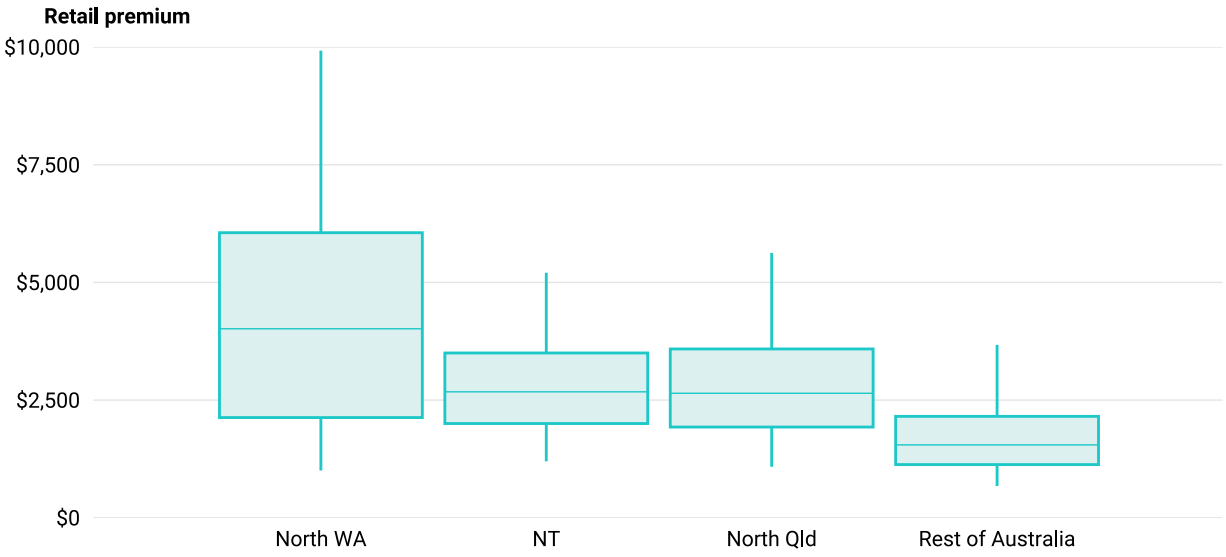
	North Western Australia	Northern Territory	North Queensland	Rest of Australia
Home and contents insurance				
Average premium	$4,395	$2,922	$2,918	$1,779
Change on previous year (nominal)	*4%*	*13%*	*7%*	*15%*
Change on previous year (real)	*–3%*	*6%*	*0%*	*7%*
Average premium per $100,000 sum insured	$716	$385	$518	$252
Strata insurance				
Average premium	$14,439	$9,826	$9,615	$6,181
Change on previous year (nominal)	*5%*	*17%*	*8%*	*20%*
Change on previous year (real)	*-1%*	*9%*	*1%*	*12%*
Average premium per $100,000 sum insured	$512	$208	$421	$145
Higher value (>$4m sum insured), median premium	$28,393	$13,245	$33,118	$10,535
Mid value ($2m – $4m sum insured), median premium	$11,172	$6,092	$7,183	$4,240
Lower value (<$2m sum insured), median premium	$3,650	$2,675	$2,138	$1,825
Small business insurance				
Average premium	$6,287	$3,670	$3,095	$1,930
Change on previous year (nominal)	*22%*	*21%*	*15%*	*15%*
Change on previous year (real)	*14%*	*13%*	*7%*	*7%*
Average premium per $100,000 sum insured	$943	$502	$630	$412

Source: ACCC analysis of data provided by insurers.
Note: The real 'change on previous year' figure is inflation adjusted, the nominal figure is not inflation adjusted. Small business insurance refers to policies for building and contents insurance.

Averages can disguise the much higher premiums paid by certain individual consumers, and our analysis confirms that premiums for properties in medium to high risk cyclone regions were considerably higher. As shown in Figure ES.1, the spread of premiums paid by policyholders can be significant, particularly in north Western Australia. For example, the figure shows that 50% of policyholders in north Western Australia paid between $2,129 and $6,057 (represented by the top and bottom border of the box) and a further 25% of policyholders paid more (and 25% paid less) than this range, as represented by the vertical lines extending above and below the box.[2] The top 5% of policyholders paid over $9,924 in north Western Australia, compared to $5,628 in north Queensland, $5,206 in the Northern Territory and $3,673 in the rest of Australia.

2 The top and bottom 5% of premiums paid are not displayed due to extreme values. See Chapter 7 for a more detailed explanation.

Figure ES.1: Distribution of retail premiums for combined home and contents insurance, by region, 2022



Source: ACCC analysis of data provided by insurers.

In 2022–23, insurers' costs to supply home and contents policies were also higher in northern Australia, largely driven by historically higher claims and reinsurance costs. While the pool seeks to reduce the cost of reinsurance for medium to high cyclone risk properties, the impact of the pool on insurers' reinsurance costs may not become evident until insurers have fully transitioned into the pool.

There can be wide variations in average annual premiums for strata policies, depending on the type, size and location of the property. To reflect this in our data, we have reported figures using a variety of measures. We broadly observed that across all sizes of strata buildings, strata premiums in northern Australia were higher and had a greater spread of prices compared to the rest of Australia. There were limited strata policies in the pool until after 1 July 2023, meaning that the effects of the pool in this market segment have not begun to emerge in our data.

Average strata premiums in 2022–23 were also highest in north Western Australia ($14,439, a decrease of 1% in real terms compared to 2021–22), followed by the Northern Territory ($9,826, an increase of 9%), and north Queensland ($9,615, an increase of 1%). The rest of Australia had an average premium of $6,181 (an increase of 12%). When measured per $100,000 sum insured, the average annual premium remained the most expensive in north Western Australia ($512, a decrease of 3%), followed by north Queensland ($421, an increase of 9%) and the Northern Territory ($208, an increase of 6%). The rest of Australia was cheapest at $145 (an increase of 13%).

As we observed with home and contents premiums, however, the price increases that strata owners faced in nominal terms appear more significant. Between 2021–22 and 2022–23, the increases were most pronounced in the rest of Australia (20%) and the Northern Territory (17%), followed by north Queensland (8%) and north Western Australia (5%).

Given the diversity in strata properties, we considered the median premiums for different sum insured values. We found that for higher value strata properties (sums insured above $4 million), policyholders in north Queensland paid the highest median premiums at $33,118, more than 3 times the rest of Australia ($10,535). For mid and lower value strata properties, median premiums were still highest in north Western Australia. Although we found average premiums to be highest in north Western Australia, of the northern regions, the vast majority of strata policies are supplied in north Queensland, meaning many more consumers are facing these prices in north Queensland.

Small business building and contents insurance premiums (for policies with less than $5 million total sum insured) rose across the country in 2022–23. As with home and strata insurance, the average

premium was highest in in north Western Australia ($6,287, an increase of 14% in real terms) followed by the Northern Territory ($3,670, an increase of 13%), and north Queensland ($3,095, an increase of 7%). The rest of Australia also increased by 7%, but from a much lower base, to $1,930. In nominal terms, these increases were 22% in north Western Australia, 21% in the Northern Territory and 15% in both of north Queensland and the rest of Australia.

Insurers' profit margins are more volatile in northern Australia, but have improved in recent years

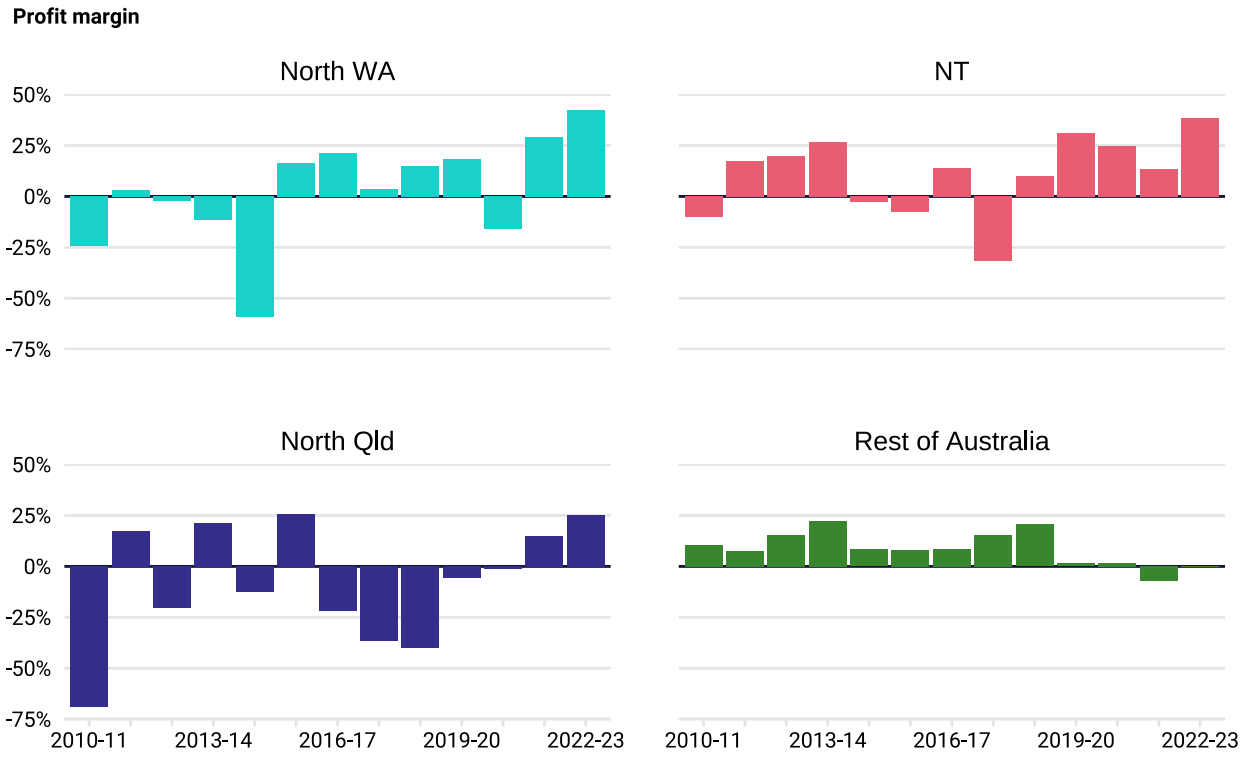
Understanding the profitability of supplying insurance in Australia is important for evaluating both the state of the industry and the impact of the pool. If northern Australian regions are consistently unprofitable despite the support provided by the pool, insurers will not be encouraged to write policies in regions of medium to high cyclone risk. This in turn will undermine the pool's objectives of lowering the price of insurance and encouraging more insurers to write in these regions. Equally, it is not intended that insurers should benefit from the pool in the form of additional profits.

Home, strata and small business insurance has recorded significant losses in recent years, but profitability appeared to recover sharply in 2022–23. While historically unprofitable, insurers operating in northern Australia have recently seen higher profit margins in those regions compared to the rest of Australia (north Western Australia 43%, the Northern Territory 38%, north Queensland 25%, and the rest of Australia breaking even at 0% for home insurance products), with parts of the rest of Australia significantly impacted by other, non-cyclone related natural disasters.

The recently improved profitability of northern Australia contrasts with sizable negative margins in the north in earlier periods. However, as shown in Figure ES.2, insurers' profit margins in northern Australia generally remain more volatile, with large variations in profit margins year on year. The rest of Australia has followed a steadier trend of mostly positive profit margins.

Profits can vary widely between insurers, but the whole industry is significantly affected by natural disasters and climate change, in addition to cyclical market conditions, such as inflation, construction costs, labour costs, the performance of the financial sector and other external factors.

Figure ES.2: Profit margin for home insurance products[3]



Source: ACCC analysis of data provided by insurers.

Consumers urgently want access to more affordable insurance

Our engagement with the community in our monitoring work continues to reinforce the importance of affordable insurance premiums to consumers across northern Australia.

In our discussions, some consumers shared optimism about the potential impact of the pool, considering that they have experienced both more choice and cheaper premiums in their area since the pool commenced. However, many have contacted the ACCC to express their worry and frustration about the impact of high and rising insurance prices, with some telling us that they have experienced increases in the order of hundreds if not thousands of dollars.

Others asked why they have not yet experienced the type of savings relief from the pool which they expected. We heard consumers say that the cost of insurance for their home or small business has become prohibitive and that they fear the pool, on its own, won't be enough to change this.

Strata owners have focused on what they perceive to be critical and ongoing affordability and availability issues in obtaining strata cover, particularly in north Queensland. Legislative requirements in states and territories for strata properties to be fully insured underlies the urgency with which these concerns are being raised.

Local and regional business and community development organisations have echoed the concerns we heard from consumers. They shared their perspectives on the impact that insurance prices are having on the liveability and economic prosperity of their broader communities.

3 'Home insurance' includes the following policy types: home building only, contents only, and combined home and contents.

Many stakeholders continue to advocate for changes to the design of the pool and additional public policy responses to address insurance affordability and availability. Some of the proposals being advocated are consistent with recommendations made in our Northern Australia Insurance Inquiry, including the provision of direct subsidies to address immediate affordability pressures; the removal or re-basing of stamp duties; and greater use of pricing that recognises disaster mitigation efforts.

Insurance pricing is complex and insurers are taking time to fully implement the pool

Insurance has traditionally been about pooling risk across consumers. However, the availability of more granular data, and more sophisticated analysis techniques, is enabling insurers to set premiums with reference to an increasing range of consumer and property characteristics.

Whilst insurers generally follow the same broad process to setting a premium, each step is complex and the approach each insurer takes can vary significantly. We found that this means insurers will not implement the pool in a uniform manner, nor necessarily in a way that will enable them to demonstrate precisely how the reinsurance pool has impacted each individual policyholder's premium.

By forgoing a margin on the reinsurance sold by the Australian Reinsurance Pool Corporation (ARPC) to insurers, the pool is designed to set cross-subsidised reinsurance premium rates. This is intended to lower the cost of reinsurance for properties at medium to high risk of cyclone, while keeping reinsurance premiums broadly comparable to what would be charged by private reinsurers for properties at low risk.

Insurers have indicated that implementing the pool is not as straightforward as them simply replacing the expected claims costs for cyclone with the ARPC's reinsurance premium. Natural peril claims modelling is complex and carving out perils covered by the pool in premium calculations needs careful consideration to ensure a close approximation of the risk.

Isolating cyclone risk from current pricing approaches is somewhat complicated by the 48-hour 'claims period'. To be covered by the pool, a loss must commence during the claims period for the cyclone event, which runs from the declared start of the cyclone event until 48 hours after the declared end of the cyclone event. Whilst not previously part of insurers' modelling, this division must now be considered so insurers can consider whether to obtain reinsurance from the private market to cover cyclone-related losses occurring more than 48 hours after the declared cyclone has ended. This, and other changes to insurers' typical reinsurance arrangements brought on by the pool, are key issues affecting timing of pool entry and implementation by insurers.

Some reinsurers have provided comments regarding their own uncertainty as to how specific mechanics of the pool will operate, and that this may not be known until fully tested by a cyclone.

Whilst insurers may experience some disruption in transitioning from their existing reinsurance arrangements to reinsuring with the pool and associated costs, the government did not expect the cost to industry to support this policy intervention to be significant.[4]

4 Explanatory Memorandum – *Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Bill 2022*, Attachment 1: Regulation Impact Statement.

Few insurers currently collect the detailed information on private mitigation which the pool is designed to incentivise

Stakeholders continue to highlight the importance of recognising and incentivising private risk reduction investments. In line with the legislative objectives of the pool, the ARPC's pricing formula includes incentives for risk reduction initiatives undertaken by homeowners, currently for roof replacement or tie-downs, window protection and roller door bracing..

However, we found that few insurers currently collect the information that would be needed to optimise this disaster mitigation design feature, and they appear to have little appetite to do so at this time.

The extent to which insurers achieve consistency with the ARPC's 'risk rating factors' will ultimately influence the extent of savings the pool will be able to generate for insurers and, ultimately, policyholders. We will monitor whether insurers improve their capability and systems over time to achieve this consistency.

Few insurers currently plan to implement a one-to-one pass-through in the short term

The legislation establishing the pool is silent as to how the ARPC's reinsurance premiums should be reflected in the premiums ultimately paid by policyholders.

While there is a widely held expectation within the community that insurers will pass on any cost savings achieved by the pool to policyholders, the ACCC has not been given the power to require insurers to take any particular approach to pass-through, nor to require insurers to communicate their approach to consumers.

Through our price monitoring role, however, we expect to provide insights about whether and how insurers are proposing to allocate savings to policies. As we watch the pool being implemented, we expect insurers to be truthful and accurate about any representations they make to consumers about how savings are being allocated. This raises questions about both insurers' ability and determination to pass through savings.

We have seen a range of intended approaches across the insurers that we are engaging with under our monitoring direction. For some insurers, their approach is still evolving. We found that few insurers currently have an intent and ability to pass-through the reinsurance price changes to consumers on a one-to-one basis following entry to the pool.

This is largely due to the magnitude of required system changes. Some insurers are planning to implement a 'phased' pass-through by initially passing on savings at a more aggregated level, before transitioning to a one-to-one pass-through approach. While a 'phased' approach may make business sense for insurers, from a policyholders' perspective it means that it will take longer for the full impact of the pool to be reflected in the individual premium they pay.

Some insurers indicated a preference to implement pass-through at an aggregated level, primarily due to limitations associated with their existing legacy systems as well as data limitations. Such an approach will invariably dampen the pool's ability to precisely target savings towards properties at medium to high risk of cyclone, as intended.

We also found that some insurers are considering the overall impact of the pool on their business and any potential flow on effects in relation to customer retention, market positioning and competitiveness.

Many insurers joined the pool throughout 2023, but price impacts will take time to play out

While participation in the pool is mandatory for certain general insurers, the legislated timeframes for joining vary. Large insurers are required to join by 31 December 2023 and small insurers are required to join the pool by the end of 2024.

Insurers' flexibility about both when they choose to join the pool and how they choose to implement it will lessen visibility of the extent of any savings across the industry and delay the timing of those savings. While the pool commenced on 1 July 2022, it wasn't until the start of 2023 that the first 2 insurers joined the pool, with most other large insurers joining the scheme around July 2023, or later.

Even after an insurer enters the pool, it will take time for changes to retail premiums to flow through to consumers.

Insurers will first need to amend their pricing methodologies and systems, which can be a resource-intensive process. Once system pricing changes have been made, they can then be reflected in premiums offered to new customers, or on renewal for those with existing policies. For most policyholders who purchase an annual policy, this means there could be a lag of up to 12 months or longer before they will see an impact from the pool from their current insurer.

We found that the time and resources involved in processing a retail price change following entry into the pool can differ among insurers. It can also add costs, particularly when significant changes are required to insurers' systems. Insurers generally expect to spread added costs associated with implementing the pool over a period of multiple years. This adds further challenges in ensuring savings are being passed on.

The pool may improve the availability of insurance for some consumers, but other barriers to entry and expansion may still remain

We found that home and contents, strata, and small business insurance markets across northern Australia are generally serviced by at least a small number of insurers.

However, there are also regions of northern Australia for which markets appear to be much more concentrated, particularly towns outside of the regional centres. This is consistent with the concerns that continue to be raised by local communities about a lack of choice of competing insurers compared to consumers elsewhere in Australia. Further, there are instances of individual properties within these regions for which insurers are not willing to offer insurance at all.

The pool is a mechanism designed to improve the availability of insurance by reducing insurers' exposure to the higher and more volatile claims costs for cyclone events. This should reduce one potential barrier for insurers' entry or expansion in northern Australia.

While there are some early signs that the pool may improve the availability of insurance in certain cyclone-prone regions for some consumers, other barriers to entry and expansion may still remain in these smaller and more regional markets.

The ACCC will continue to monitor prices, costs and profits and collect further data to inform the assessment of the pool

Over time, our monitoring will establish a data set to help examine the impact of the pool on prices, costs and profits of insurance, and inform views and expectations about its effect. Ultimately, this work should allow governments to evaluate whether the pool is in fact operating and delivering outcomes as intended.

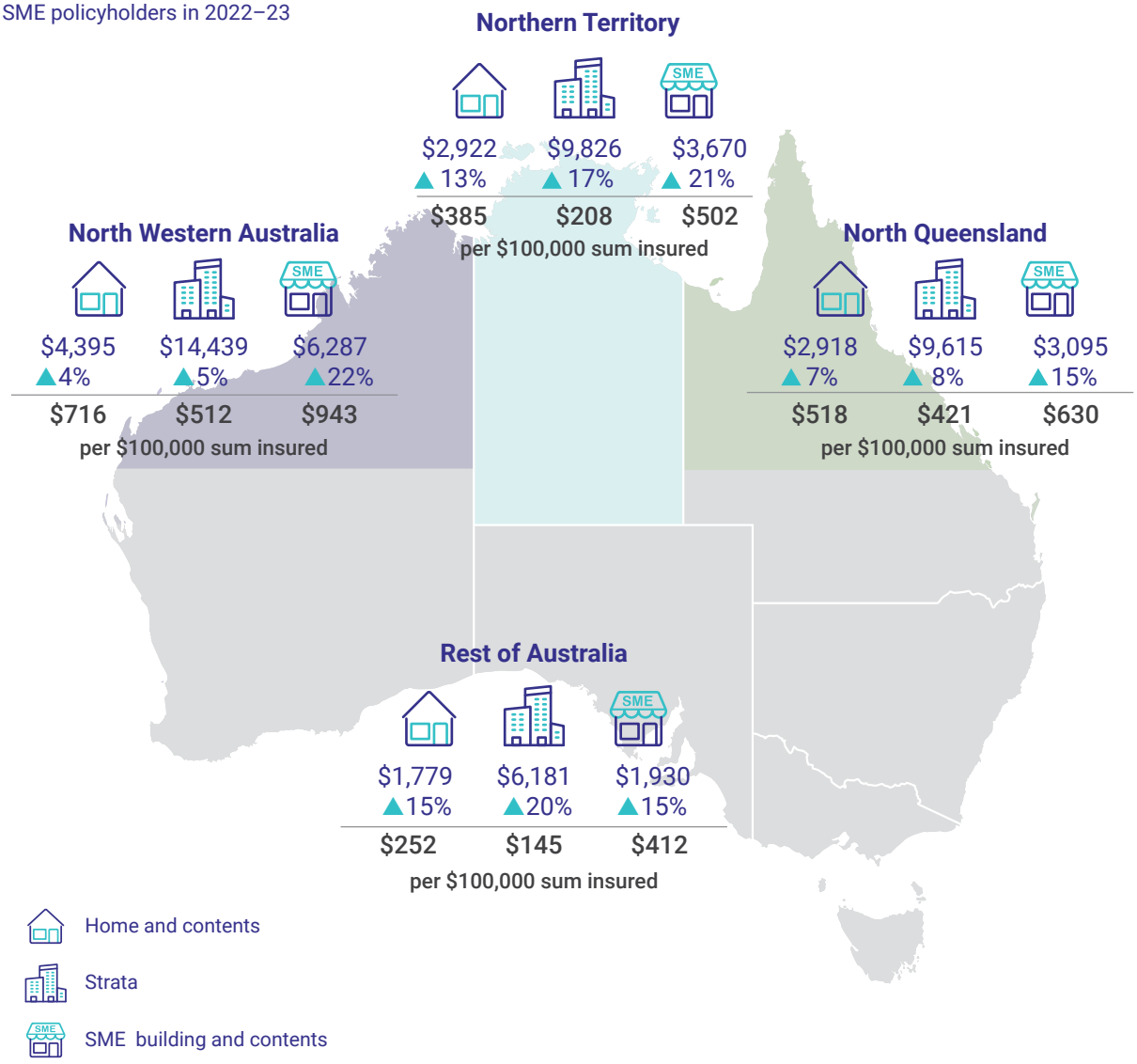
With more insurers joining the pool through 2023–24, we expect our 2024 reporting to examine the early effects of the pool on insurers' prices, costs and profits. Nonetheless, it still may be some time before the full effects of changes to prices and choice are seen across the industry, and it may be difficult to isolate the effects of the pool from the range of other factors impacting insurance markets.

We will continue to complement our core monitoring task with a deeper examination of particular issues the pool is designed to address, such as availability of insurance in strata markets. We will also continue to support related government initiatives which seek to better understand and improve insurance outcomes for communities at risk of natural disasters more generally.

Insurance monitoring snapshot 2022–23

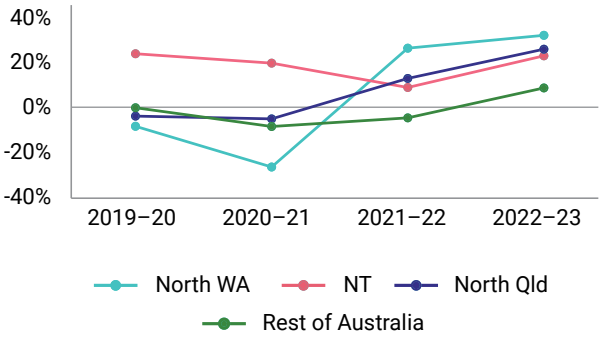
Average premiums

Prices faced by home, strata and SME policyholders in 2022–23



Profit margins

Home, strata, and SME insurance products



Reinsurance as a proportion of insurers' costs to supply insurance

Home, strata and SME insurance products in 2022–23

Northern Australia	43%	44%	21%
Rest of Australia	16%	20%	13%

1. Background

This chapter describes the ACCC's insurance monitoring role and provides background on the government's cyclone reinsurance pool.

1.1 The ACCC's role in insurance monitoring

1.1.1 Direction to monitor prices, costs, and profits

On 12 January 2022, the then Assistant Treasurer issued a direction to the ACCC under subsection 95ZE(1) of the *Competition and Consumer Act 2010* (Cth). The object of the direction is for the ACCC to monitor prices, costs and profits relating to the supply of certain insurance cover before and after the introduction of the cyclone and related flood damage reinsurance pool (the pool).[5] The pool is discussed in more detail in Section 1.2 of this report. We are directed to give special consideration to monitoring the prices, costs and profits relating to the supply of insurance cover in respect of the destruction of, or damage to, one or more of the following:

- a home building
- contents of residential building
- a strata title residence
- commercial premises, and contents of those commercial premises, if the total sum insured does not exceed $5 million.[6]

The then-government stated that the pool is designed to improve the accessibility and affordability of insurance for households and small businesses in cyclone-prone areas across Australia.[7] The government also expected the pool to increase insurer participation in insurance markets in northern Australia, increasing competition and putting further downward pressure on premiums.[8]

The ACCC is to collect data to evaluate the impact of the pool, and assess whether savings from the pool are being passed through to policyholders, and whether the pool is delivering on its intended outcomes.[9] As discussed in Chapter 5, there is a spectrum of approaches to pass-through being used by insurers at present. Our monitoring will continue to provide transparency and analysis on this issue, which is critical to assessing whether the pool is achieving its intended outcomes for insurance consumers.

Under the direction, the ACCC is required to report on its monitoring at least once every calendar year from 2022 until 30 June 2026.

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5 Australian Government, *Competition and Consumer (Price Monitoring – General Insurance Policies) Direction 2022*, Federal Register of Legislation website, 12 January 2022, paragraphs 5–6.

6 Australian Government, *Competition and Consumer (Price Monitoring – General Insurance Policies) Direction 2022*, Federal Register of Legislation website, 12 January 2022. Section 7(b), (c) and definition of 'covered insurance policies' in section 4. While parametric insurance products can complement, or in some cases be used as a substitute for, some general insurance products, these products are not within the scope of our direction.

7 Australian Government, The Treasury, *Government releases exposure draft legislation on the reinsurance pool* [media release], 3 December 2021, accessed 26 June 2023.

8 Australian Government, The Treasury, *Morrison Government passes legislation to deliver reinsurance pool* [media release], 30 March 2022, accessed 26 June 2023.

9 Australian Government, The Treasury, *Government releases exposure draft legislation on the reinsurance pool* [media release], 3 December 2021, accessed 26 June 2023; Australian Government, The Treasury, *Fact Sheet: Reinsurance pool for cyclones and related flood damage*, February 2022, accessed 26 June 2023.

1.1.2 ACCC's first monitoring report (December 2022)

On 20 December 2022, we released our first insurance monitoring report (first report). At the time of publishing that report, although the pool had commenced on 1 July 2022, no insurers had joined the pool. Accordingly, our first report focused on:

- the background and context to the introduction of the pool and the ACCC's monitoring role
- market developments
- prices and costs in residential, strata and small business insurance
- insurers' proposed approach to implementing, and views on, the pool.

A copy of the report can be found here on the ACCC's website: Insurance monitoring report 2022.

1.1.3 Northern Australia Insurance Inquiry

This report, and our monitoring task, indirectly follows the ACCC's previous work on insurance affordability and availability in northern Australia. In 2017, the Australian Government directed the ACCC to conduct a wide-ranging inquiry into the supply of residential building, contents, and strata insurance in northern Australia. In addition to considering the prices, costs and profits of northern Australian insurance markets, the ACCC also explored a range of other factors which may be limiting the effectiveness of these markets for consumers, for example barriers to entry and expansion, impediments to informed consumer choice, conflicts of interest, land use planning, building specifications, and approaches to managing payment difficulties.

The inquiry began in July 2017 and concluded in December 2020 with the publication of the Northern Australia Insurance Inquiry final report (the NAII final report). The NAII final report brought together significant analysis and recommendations from the 3-year inquiry on the operation of the markets for residential, contents and strata insurance in northern Australia.

The ACCC made 38 wide-ranging recommendations across 6 categories to governments and industry to address the concerns we identified, and to help improve competition and consumer outcomes in northern Australian insurance markets through a variety of means:[10]

- **Making it easier to search for, and compare, insurance products**

  We considered that there were a range of reforms that would make it easier for consumers to search for, and compare, insurance products. We recommended changes to improve the comparability of insurance products, require insurers to share certain information with consumers and make it easier for consumers to access existing information sources.

- **Choosing the right amount of cover**

  Consumers generally bear the risk of underinsurance, as they are required to nominate the sum insured for their property. We considered that insurers could provide clearer advice to their customers to help them choose the level of cover that they need.

- **Dealing with conflicts of interest**

  Conflicts of interest are common and significant for both insurance brokers and strata managers. We made 3 recommendations to address these conflicts.

10 ACCC, *Northern Australia Insurance Inquiry – final report*, (NAII final report), 28 December 2020, pp 17–31.

- **Improving consumers' rights**

  We made a number of recommendations to empower and better protect consumers in their dealings with insurers, particularly when they are experiencing financial difficulty or need to make a claim on their insurance.

- **Reducing risk and building better**

  Improving the resilience of properties and communities to natural hazards will have significant benefits now and into the future, including through lower insurance claims costs. We considered that greater consideration of the likely benefits (and costs) of mitigation and other resilience measures is required.

- **Addressing immediate affordability concerns**

  We found that reforms to remove or re-base state and territory stamp duties on home, contents and strata insurance products had the potential to immediately relieve pricing pressure for all consumers in northern Australia. We considered a range of more direct interventions that governments could take, finding that direct subsidies would have the greatest potential to work in a targeted way to relieve some of the acute insurance affordability and cost of living pressures for households in these regions.

The ACCC considers that many of the findings and recommendations from the NAII final report remain relevant today. Since the NAII final report, there have been various public policy responses and decisions from governments on insurance issues (discussed further in Chapter 2), some of which address aspects of the ACCC's 38 recommendations. This includes the establishment of the pool. However, to date, there has been no formal government response to the recommendations made by the ACCC in the Northern Australia Insurance Inquiry.

1.2 About the cyclone reinsurance pool

1.2.1 Development of the pool

Following widespread concern about the cost of insurance for households and small businesses in northern Australia, the Australian Government announced its intention to establish a reinsurance pool for cyclone and related flood damage on 4 May 2021.[11]

On 31 March 2022, the *Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Act 2022* came into force, amending the renamed *Terrorism and Cyclone Insurance Act 2003* (Act). The Act established a framework for a cyclone and related flood damage reinsurance pool to be administered by the Australian Reinsurance Pool Corporation (ARPC).

Purpose of the pool

The Explanatory Memorandum to the amending legislation explains the context for the establishment of the pool:

> The damage to residential and business property caused by extreme weather events, including cyclones, can be severe and on a scale that leads to the displacement of people from their homes and disruption to business activity. Due to the greater risks of extreme weather events in cyclone-prone areas, insurance premiums are significantly more expensive.

11 Explanatory Memorandum – *Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Bill 2022* (Explanatory Memorandum) [1.6]; Australian Government, *More affordable access to insurance for Northern Australians* [media release], 4 May 2021, accessed 31 August 2023.

> This has led to cover becoming less accessible and affordable for households and small businesses in these regions. Households that are underinsured or have no insurance have reduced financial capacity to recover from a natural disaster or other event. Poor insurance coverage can exacerbate costs and pressures for communities and for governments through increased pressure on health, emergency and welfare systems. It can slow the economic recovery of a region following a disaster.[12]

Against this background, the Australian Government established the pool for the purpose of 'improving insurance access and affordability for households and small businesses in cyclone-prone areas in Australia.'[13]

To achieve this purpose, the pool is:

> designed to lower insurance premiums for households and small businesses with high cyclone and related flood damage risk by reducing the cost of reinsurance, which is a significant cost component of premiums for these policies.
>
> The scheme would allow insurers to reinsure cyclone risks at a lower cost than in the private reinsurance market as it is designed to be cost-neutral to the Government over time and be backed by a Commonwealth guarantee.[14]

That is, unlike private reinsurers, the ARPC would not seek to achieve a profit when providing reinsurance for cyclone risks to insurers.

Box 1.1: Reinsurance and government reinsurance pools explained

Reinsurance is effectively insurance for insurers. Insurance works by pooling and spreading risks to mitigate their impact: insurers collect (relatively smaller) premiums from their many policyholders and pay out (relatively larger) claims if insured events occur. This is how insured risks are mitigated.[15]

Similarly, reinsurance is designed to protect insurers from large financial losses when paying out claims to policyholders. In return for transferring risk to reinsurers, insurers pay reinsurance premiums. The role and types of reinsurance is discussed further in Section 4.2.2.

A government reinsurance pool is an entity which is owned, run, funded and backed by government, and offers reinsurance to insurers for specific risk types (such as cyclones).[16] The design elements of a reinsurance pool can vary. Typically, insurers pay a reinsurance premium to transfer risks associated with particular perils to the pool.

12 Explanatory Memorandum [1.3]–[1.4].

13 Explanatory Memorandum [1.1].

14 Explanatory Memorandum [1.7]–[1.8].

15 Productivity Commission, *Competition in the Australian Financial System – Inquiry report*, no.89, 29 June 2018, p 388, accessed 15 November 2023.

16 ACCC, *NAII final report*, p 156.

Key features of the legislative framework

The Act and associated regulations prescribed in the *Terrorism and Cyclone Insurance Regulations 2003* set out key features of the pool's coverage and scope, including when an insurer must join the pool, and the types of insurance and weather events covered by the pool.

In general terms, insurers must enter a reinsurance agreement with the ARPC if the insurer writes more than $10 million in gross written premiums in regions of cyclone risk for:

- residential home and contents, including landlord insurance and farm residential buildings[17]
- residential strata[18]
- commercial strata and small business insurance with a maximum of $5 million total sum insured across property, contents and business interruption.[19]

The pool will cover 100% of the expected claims costs for all eligible cyclone losses (above the policyholder's excess) for eligible policies.[20] Broadly, eligible cyclone losses are losses caused by a weather system declared to be a 'cyclone event' by the ARPC, on the advice from the Bureau of Meteorology.[21] The losses can arise from any of the following:

- wind, rain, rainwater, rainwater run-off
- storm surge
- flood.[22]

As required by the legislation, the ARPC has developed a process for formally declaring the beginning (or re-intensification) and the end of a cyclone as soon as reasonably possible, based on the Bureau of Meteorology's advice (referred to as 'the cyclone event').[23]

To be covered by the pool, the loss must commence during the claims period for the cyclone event.[24] The claims period, as defined in the legislation, runs from the declared start of the cyclone event until 48 hours after the declared end of the cyclone event.[25]

The pool is to be funded by reinsurance premiums paid by insurers to the ARPC and supported by a $10 billion annually reinstated Commonwealth guarantee, which can be increased by the relevant Minister.[26]

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17 For information on farm pack policies, see Australia Reinsurance Pool Corporation (ARPC), *Cyclone Pool FAQs – What classes of business are eligible for the cyclone pool?*, ARPC website, n.d., accessed 28 August 2023.

18 Residential strata includes mixed-use strata schemes, where 50 per cent or more of floor space is used mainly for residential purposes: *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8B(3)(c); *Terrorism and Cyclone Insurance Regulations 2003* (Cth) r.4A.

19 *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8B(3)(c); *Terrorism and Cyclone Insurance Regulations 2003* (Cth) r.5B(10).

20 'The pool will cover all eligible claims (above the policyholder's excess) for cyclone claims for the first 3 years. Thereafter, the pool will operate on a risk-sharing arrangement with insurers to allow a staged transition to a limited level of risk retention by insurers. The level of risk retention will be set by Ministerial direction and will be informed by consultation with insurers': *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8A , 8B and ss38(2)(e); Explanatory Memorandum [1.91].

21 Under this section of the *Terrorism and Cyclone Insurance Act*, the Bureau of Meteorology must notify the ARPC if it determines that a cyclone exists (or has reintensified after being downgraded to an ex- or post-tropical cyclone) and is likely to affect any part of Australia, and again once the cyclone ends. 'Cyclone' is defined in regulation 3A of the *Terrorism and Cyclone Insurance Regulations*. *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8B(3)(c); *Terrorism and Cyclone Insurance Regulations 2003* (Cth) r.3A.

22 *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8C; *Terrorism and Cyclone Insurance Regulations 2003* (Cth) r.5C(2).

23 *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8E and 8F; ARPC, *Declarations – Cyclone declarations*, ARPC website, n.d., accessed 5 September 2023.

24 *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8C(3).

25 *Terrorism and Cyclone Insurance Regulations 2003* (Cth) r.5D.

26 *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.35(a).

When setting the reinsurance premiums that insurers must pay, the ARPC must seek to: [27]

- ensure that reinsurance premiums are sufficient over the longer term to meet its costs and liabilities
- keep premiums as low as possible while maintaining incentives to reduce and mitigate the risk of eligible cyclone losses for eligible policies with medium to high levels of exposure to eligible cyclone losses
- keep premiums at comparable levels to what would be charged by other reinsurers for eligible policies with lower levels of exposure to eligible cyclone losses.

By requiring the ARPC to incorporate incentives for properties that have undertaken action to mitigate the risk of cyclone and relating flooding, the government hopes that, over time, these discounts will help to improve the affordability and sustainability of property insurance.[28] The extent to which the pool incentivises this mitigation activity will depend in part on the way insurers themselves collect information about mitigation and reflect it in consumer pricing.

The legislation is silent on how the ARPC's reinsurance premiums should be reflected in the premiums ultimately paid by policyholders and whether or how insurers should pass on any savings from the pool to policyholders. However, the then government set the expectation, including through its announcements about the passage of the Act and on the ACCC's monitoring role, that savings will be passed onto policyholders.[29]

Participation in the pool is mandatory for general insurers with a sufficient value of eligible policies. Large insurers must join the pool by 31 December 2023. Small insurers must join by 31 December 2024.[30] Insurers have flexibility in transferring their eligible policies to the pool ahead of the mandatory transition date. Insurers can progressively transfer their policies into the pool on a rolling basis, transfer their whole portfolio in a bulk transfer, or a combination of both, as long as it is completed by their relevant transition date.[31]

The Act does not require insurers to provide cyclone coverage to consumers or to participate in northern Australian insurance markets. Rather, the Act requires any insurer that *does* provide certain types of insurance cover and meets certain thresholds, described above, to join the pool and obtain reinsurance from the ARPC.

While insurers must participate in the pool if they meet the above thresholds, they are not prevented by the legislation from obtaining additional reinsurance from the private market for any retained risks that are not transferred to the ARPC.[32] After joining the pool, insurers may still need to obtain private reinsurance cover in respect of any cyclone-related risks not covered by the above definitions (such as flooding that commences outside the claims period). Insurers will also continue to need reinsurance for non-cyclone related losses (such as from bushfire, earthquakes or non-cyclonic flood).

Chapter 5 discusses in detail how the pool is operated, how reinsurance premiums are set by the ARPC (including mitigation incentives), and the expected savings to be generated from the pool.

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27 *Terrorism and Cyclone Insurance Act 2003* (Cth) ss.8D.

28 Explanatory Memorandum [1.88].

29 Australian Government, The Treasury, *Government releases exposure draft legislation on the reinsurance pool* [media release], 3 December 2021, accessed 26 June 2023; Australian Government, The Treasury, *Morrison Government passes legislation to deliver reinsurance pool* [media release], 30 March 2022, accessed 26 June 2023.

30 For the transitional provisions, a general insurer is large if its gross written premiums were $300 million or more for the household direct business, as reported to APRA, or small if its gross written premiums were under $300 million.

31 For more information on transition consideration, see ARPC, *Cyclone Reinsurance Pool Insurance Company Onboarding Guide as at 15 December 2022 [PDF 490KB]*, accessed 28 August 2023.

32 Explanatory memorandum [1.15].

1.2.2 Commencement of the pool

The pool commenced operation on 1 July 2022. Insurers' entry to the pool is discussed in more detail in Chapter 3 but, in summary, as at November 2023, 11 insurers had joined the pool.

Since the commencement of the pool, the ARPC has declared 4 cyclone events:

- Tropical Cyclone Ilsa
- Tropical Cyclone Gabrielle
- Tropical Cyclone Ellie
- Tropical Cyclone Darian.[33]

1.3 Sources of information for this report

We have drawn on various sources of information to inform this report.

This report includes information and data the ACCC previously collected for our Northern Australia Insurance Inquiry and now collects under our monitoring role. Additionally, we have drawn on publicly available reports and sources of information and discuss these where relevant throughout this report.

Stakeholder engagement

To help inform our approach to fulfilling this monitoring role, we have engaged with a range of stakeholders with important lived experience of insurance premium pressure or a particular industry expertise (and often both). In addition to receiving direct consumer concerns and inquiries from across northern Australia, we have also met with local councils, consumer representative groups, strata representative groups, regional and economic development committees, regional chambers of commerce, insurance brokers and elected representatives.

We conducted our engagement through face-to-face and online meetings, phone calls and email correspondence.

We thank all the individuals and groups who have raised their concerns and shared their insights and expertise with the ACCC. The insights from stakeholder consultations have usefully informed our approach to the analysis throughout this report.

The ACCC welcomes receiving information directly from consumers and local communities about their experiences of insurance affordability and availability, and the impact that this has on their household, small business or community. We can be contacted via email at insurancemonitoring@accc.gov.au.

Information collected from insurers

We used our compulsory information gathering powers under section 95ZK of the Competition and Consumer Act 2010 to obtain information, data and documents from 21 insurers. These insurers supply home and contents, strata, and small business insurance in regions considered to be at risk of cyclone and cyclone-related flood damage in Australia. There may be other insurers operating in these regions who we have not obtained information from, but these are likely to be small in number.[34]

33 ARPC, *Declarations – Cyclone declarations*, ARPC website, n.d., accessed 26 August 2023.

34 The insurers we have collected from account for over 86% of gross written premium for general insurance institutions (direct insurer) for the financial year ending June 2023. APRA, *Quarterly general insurance institution-level statistics as at 30 June 2023*, 24 August 2023, accessed 6 Sept 2023.

Penalties apply under section 137 of the *Criminal Code* (Cth) for anyone who knowingly provides information that is false or misleading to a Commonwealth entity in response to a notice.

To inform the analysis and observations in this report, we collected information from the following insurers:

- AAI Limited (Suncorp)
- Achmea Schadeverzekeringen N.V.
- AIG Australia Limited
- Allianz Australia Insurance Limited
- Ansvar Insurance Limited
- Auto & General Insurance Company Limited
- Chubb Insurance Australia Ltd
- Defence Service Homes Insurance Scheme
- Guild Insurance Limited
- The Hollard Insurance Company Pty Ltd
- Hollard Insurance Partners Limited (formerly Commonwealth Insurance Limited)[35]
- Insurance Australia Limited and Insurance Manufacturers of Australia Pty Ltd (together, Insurance Australia Group)
- Liberty Mutual Insurance Company
- Pacific International Insurance
- QBE Insurance (Australia) Limited
- RAC Insurance Pty Ltd
- RACQ Insurance Limited
- Sure Insurance Pty Ltd[36]
- Youi Pty Ltd
- Zurich Australian Insurance Limited.

Broadly, we collected data, documents, and information from the insurers listed above, about the following:

- data on insurance policies, claims, and financial information
- the process of setting insurance premiums
- any embargoes and exposure limits in place
- current reinsurance arrangements
- their approach to implementing the pool
- expectations as to the impact of the pool.

35 Our first insurance monitoring report contains data from Commonwealth Insurance Limited for a period prior to its acquisition by Hollard Group on 30 September 2022. From 1 October 2022, Commonwealth Insurance Limited has been renamed Hollard Insurance Partners Limited. Hollard Insurance, *New Insurance Partnership: About Hollard and the Commonwealth Bank*, Hollard website, n.d. accessed 28 June 2023.

36 Sure Insurance Pty Ltd is not an insurer, but a managing general agency underwriting policies for its product issuers, Liberty Mutual Insurance Company, and Pacific International Insurance. Data on insurance policies and claims used in this report considers the 3 entities together as one insurer.

We also spoke to other insurers in addition to those above that we obtained data and documents from.

Data, limitations and assumptions

We aligned the insurance policy data collected during our monitoring role with the types of insurance policies that are covered by the pool (see Section 1.2.1 for information about coverage of the pool).

Where possible and appropriate, we have also compared data collected under our current direction with data collected during the Northern Australia Insurance Inquiry, and continued or extended relevant data series. Data for prices, costs and profits collected during the Northern Australia Insurance Inquiry covered the period 2008 to 2019. Given this time period, and the commencement of data collected under this role, some time series data presented in this report does not include the financial years 2019 to 2021. The actual movements within those intervening years may be different to the trend line presented. This is noted where relevant.

Further, there are differences in the scope of data collected between the Northern Australia Insurance Inquiry and our current monitoring role. This includes, but is not limited to:

- the number of insurers from which information was sought. The Northern Australia Insurance Inquiry primarily collected information from 8 of the largest insurers providing insurance in northern Australia at the time of that inquiry. Our current role has sought information from these same insurers, and a number of additional insurers as outlined above[37]
- the types of insurance policies. Small business insurance was not within the terms of reference for the Northern Australia Insurance Inquiry and hence, no historical data series is available from that inquiry.

There may also be small changes to data, definitions, or calculations between the 2 collections, particularly across different insurers. For these reasons, comparisons over time should be interpreted with caution.

In this monitoring task, we have collected detailed premium information from insurers for the purposes of providing estimates of the components which comprise retail premiums. This policy level data was collected for contracts in effect (active contracts of insurance) as at 30 September 2022; a time before any insurers had joined the pool. This data in combination with the time series information from the Northern Australia Insurance Inquiry enables us to establish a baseline. We will continue to collect and update this information for the duration of our monitoring role.

There are instances throughout this report where we identify insurers by a number, rather than their name. The allocation of an identifying number is random and not consistent between sections of analysis. That is, 'Insurer 1' will not be the same insurer across all charts where this label is used.

Our analysis relies on the availability and accuracy of information and data supplied by insurers. Insurers' systems and processes to record their data can vary widely depending on how they approach pricing (see Chapter 4), the sophistication of their data systems, and other factors. We have collected data in a standardised format which has meant that insurers may have made varying assumptions in preparing the data. In some cases, insurers were unable to provide data as requested, or had to rely on estimates to do so. In some cases, we have not been able to include data from all insurers we collected from. This is noted in the report where relevant.

We have conducted quality assurance processes on all data provided by insurers and have confidence in the findings presented throughout this report. We have sought independent verification of our calculation methodologies where appropriate. Data limitations and assumptions are discussed in further detail in Appendix A.

37 See Appendix A for a comparison of the insurers from which the ACCC collected information during the Northern Australia Insurance Inquiry and under this monitoring role.

Where we have presented analysis in real 2023 dollars, we have used the All Groups Australia Consumer Price Index to adjust older data for inflation.[38] For this reason, figures presented in earlier reports may not align with what is presented in this report.

Information from reinsurers

Since our first monitoring report, we also engaged with several reinsurers with operations in Australian markets. In June 2023, we also issued a voluntary information request to, and received responses from, 5 reinsurers seeking to understand the effect of the pool on their operations, including the impact on 2023 reinsurance renewals and the costs associated with providing reinsurance. Those reinsurers are:

- General Reinsurance Australia Ltd
- Hannover Rück SE
- Munich Reinsurance Company
- RenaissanceRe
- Swiss Re Asia Pte. Ltd., Australia Branch.

We note there are many other reinsurers providing natural catastrophe reinsurance to Australian insurers, many of which are primarily based overseas. Accordingly, the information discussed in relation to reinsurers' views is not necessarily representative of all reinsurers' views.

38 Australia Bureau of Statistics (ABS), *Consumer Price Index, Australia, June Quarter 2023*, ABS website, n.d., accessed 6 October 2023. See Appendix A for more information about our inflation adjustment methodology.

2. Insurance market conditions

High and rising insurance prices are attracting an increasing sense of concern and attention around the country. We continue to hear from consumers in northern Australia that insurance premiums are unaffordable.

Our task is to monitor the prices, costs and profits of eligible insurance policies, with regard to the impact of the pool. However, we recognise there are many social, economic, and environmental issues beyond the pool, both locally and globally, that are influencing the insurance premiums facing Australian consumers. These issues are being examined by a variety of different processes and with different focuses.

While damage to property from tropical cyclones in 2022–23 was relatively minimal, other extreme weather events have had an ongoing impact since our first report in December last year. Many communities across Australia are still recovering from the impacts of catastrophic flooding, with insurers handling high claims volumes and claims costs.

To provide context for the analysis in this report, this chapter looks at some of the broader factors influencing the insurance markets and outcomes for consumers. In Section 2.1, we reflect on the feedback that we continue to hear from communities in northern Australia about the challenges they face in obtaining insurance. In Section 2.2, we note a range of inquiries, reports and programs being undertaken by others which seek to further consider or address insurance affordability, disaster resilience and preparedness, and improving outcomes for consumers. In Section 2.3, we provide an overview of some of the other external economic and environmental pressures influencing insurance premiums.

2.1 Community sentiment and concerns

The lived experiences of consumers can be a reflection of how markets are functioning and provides an important context for the prices, costs and profits data we report on.

Our engagement with the community through our monitoring work continues to reinforce the importance of affordable insurance premiums to consumers across northern Australia and has emphasised their high expectations around the savings that the pool may deliver. While it is still early in the implementation of the pool, we have heard from some consumers who have welcomed their experience of more choice and a reduction in premiums following the commencement of the pool. However, we have also heard others say that the cost of insurance for their household or business has become prohibitive and that they don't expect the pool, on its own, will be enough to change this.

The concerns we have heard are broader than just the potential impact of the pool on prices; we have also heard concerns and proposals more akin to the wide-ranging market issues that we considered as part of our 2017–2020 Northern Australia Insurance Inquiry, such as the effects of stamp duty, commission structures, land use planning and building specifications. We consider that many of the findings and wide-ranging recommendations that we made as part of that inquiry continue to remain relevant, and the community feedback we have heard confirms this.

We thank all the individuals and groups who have raised their concerns and shared their insights with the ACCC, some themes of which are summarised below. We welcome contact from communities across northern Australia and can be contacted via email at insurancemonitoring@accc.gov.au.

2.1.1 Local residents and property owners

Most consumers who contacted us have consistently expressed their frustrations and concerns about the impact of high and rising insurance prices. Some consumers have mentioned experiencing premium increases in the order of hundreds if not thousands of dollars compared to the previous year. Some have asked why they have not experienced the savings relief from the pool which they expected. However, others have shared their optimism about the potential impact of the pool, observing they have experienced both more choice of insurers and a reduction in premiums.

Several consumers have said that insurers should be required to explain how premiums are set and why they are changing. Some want to understand why they are paying more than what they think is fair, given what they believe is the relative risk of their property. Consumers have also called for more transparency from insurers about the impact of the pool and how their insurer has passed on any savings to them.

We have also heard consumers say they had to adjust their coverage levels and increase their excess to improve affordability and others accept they face the prospect of being uninsured. Consumer representative groups expressed strong concern about the impacts of non-insurance and underinsurance.

Strata owners, particularly in Townsville, have engaged strongly and constructively with the ACCC. Representations from strata owners have focused on concerns of critical affordability and availability issues in obtaining strata cover, particularly in north Queensland. Whilst legislative requirements to fully insure strata properties underpins the urgency of access to affordable insurance, these requirements also protect those owners from the risks of non-insurance. Owners have discussed with us that the need for some bodies corporate to resort to purchasing industrial special risk policies and policies sold by offshore insurers highlights the difficulties that some strata buildings are experiencing in buying compliant strata policies from Australian markets.

Similar to concerns raised by home building owners, some strata owners who engaged with the ACCC have called for more transparency from insurers in the way the insurance is priced, particularly in relation to natural disaster risk and the range of other working claims which are typically covered by a strata policy. One strata representative group has advocated for greater transparency of the procurement of strata insurance, which is typically intermediated by a range of third parties acting on behalf of each of lot owners and insurers.

Conflicts of interest between strata managers and brokers based on commission-based remuneration continues to be raised as a concern. The removal of stamp duty and other taxes on insurance continue to be flagged as opportunities to reduce premiums, including in reports and positions published by other stakeholders (see Section 2.2.1).

2.1.2 Local councils, regional development committees and regional chambers of commerce

The local councils, regional development committees and regional chamber of commerce groups that we spoke to across northern Australia shared similar concerns about price and choice of insurance. However, in doing so, they focused more on the overall impact that insurance prices are having on the liveability and economic prosperity of communities more generally.

For example, one group we spoke to highlighted the challenges of meeting local housing demand due to an inability to get insurance for medium density high rise (strata) buildings. This has flow on effects for communities trying to attract and retain workers. Rising insurance costs may also contribute to landlords raising rents, further pressuring tenants.

Several regional development groups reflected on the cost of insurance almost certainly contributing to the closure of prominent local businesses, which not only has a direct economic impact, but also hurts local community spirit. One group specifically spoke about insurance prices being a deterrent for attracting investment to their region. Several stakeholders spoke of local businesses they knew of operating without insurance, either because they simply could not get insurance or just could no longer afford it, and the risk this exposed them to. One group raised specific concerns about the impact of unaffordable insurance in remote communities whose economic activity helps to sustain and support communities with large Indigenous populations.

When meeting regional groups, we often invited any insights about the level of awareness of the pool among their respective local communities. The answers we received varied. In north Queensland, where some larger insurers joined the pool earlier, community awareness appeared higher and more locals spoke of increased choice and price reductions. Some queried whether the pool was actually going to save any money, or just cause prices not to increase it as much as they otherwise would. Further to the west, there was a greater sense that an initial anticipation of a positive impact had receded, with individuals not experiencing savings of the type they had hoped for.

The role of land use planning, building specifications, risk mitigation and the impact of stamp duties were recurring themes of interest among these types of groups. Some groups questioned whether there was still scope for recommendations made by the ACCC in our Northern Australia Insurance Inquiry to be considered. As noted above, we consider that many of the findings and recommendations from the NAII final report remain relevant today.

2.1.3 Insurance brokers

We engaged with a range of local brokers as well as larger broker groups, to understand brokers' observations about insurance conditions in local markets and views on the pool. Brokers provided a range of views based on their own experiences of doing business but also reflected views which have been informed by way of feedback from their clients living and doing business in northern Australia.

Brokers raised similar issues to those we heard from other groups, particularly around the lack of choice and affordability of insurance in northern Australia, along with related concerns around increasing trends of underinsurance and non-insurance. One broker provided some specific examples of the impact of under-insurance on clients who had suffered substantial losses.

Some brokers noted the limited number of insurers writing business in parts of northern Australia for some insurance products and, relatedly, a large disparity in the prices that different insurers might be offering for the same risk. Affordability and availability concerns were also discussed in relation to insurers' increased use of risk-based pricing and tightening underwriting guidelines.

Discussing the impact of the pool, some noted an initial sense of optimism and high expectations from their clients around the potential impact of the pool, which for some clients had shifted to a sense of frustration. One broker group considered the pool is likely to have a positive impact on premiums but noted that there will be a delay before pricing changes arising from the pool will take effect.

2.2 Insurance policy developments

Since our first report was published in December 2022, there have been several inquiries, reports and programs undertaken by governments, regulators, industry and consumer stakeholder groups to further consider and/or address disaster resilience and recovery, insurance affordability, insurers' internal systems, and outcomes for insurance consumers. Some of the concerns in these reports echo concerns raised more directly with us by stakeholders.

This section outlines some of these pieces of work and notes their relevance to our monitoring work and the pool. While some of the current challenges facing insurance markets extend beyond the pool and the impact of cyclone risk on insurance premiums, these reports give an important consumer context to insurers' reported experiences in the current market, discussed in Section 2.3 below.

As already noted above, our Northern Australia Insurance Inquiry was a wide-ranging investigation into the availability and affordability of home, contents and strata insurance, and we consider that many of the findings and recommendations we made in the final report of that inquiry remain relevant today. In addition to providing the government with an important evidence base as to how the pool is working, we will continue to actively contribute to the broader public discussions about insurance issues more generally, where we have expertise to do so.

2.2.1 External policy reports

Insurance affordability and extreme weather events

Various groups have reported increasing insurance affordability pressures across home building, contents and strata insurance, reflecting concerns raised with us by communities. The level of ongoing public and policy discussion on the interconnected issues of insurance and extreme weather is to be expected given the complexity of the issues and the profound impacts on Australians' lives and livelihoods.

A changing climate, which many expect to exacerbate extreme weather events in future, has heightened concerns about access to affordable insurance. According to the Bureau of Meteorology, Australia is projected to experience fewer tropical cyclones, but a greater proportion are projected to be of high intensity, with large variations from year to year.[39]

In August 2023, the Actuaries Institute reported that affordability pressures have risen for almost all Australian households since its 2022 green paper, with a 28% increase in the median home insurance premium in the year to March 2021, which was not matched by household income growth.[40] The proportion of 'affordability stressed' households rose from 10 to 12%, with those households spending an average 8.8 weeks of income on home insurance.[41] The Institute reported that flood risk, in particular riverine flood, played a significant role in the current pressure on home insurance affordability.[42]

Similarly, a joint report from CHOICE in collaboration with consumer and climate groups in August 2023 reported that insurance premiums are becoming increasingly unaffordable for people living in disaster-prone areas, with many households on low incomes being priced out of the insurance market entirely.[43] In a nationwide survey of home and contents insurance policyholders, 87% reported a rise in their premium at their most recent renewal. CHOICE also reported on other challenges facing insurance consumers, include complex product design, inaccessible information on natural hazard risk, and high-risk areas of Australia requiring solutions beyond insurance, including planned relocation.[44]

39 Bureau of Meteorology, *State of the Climate 2022 – Future Climate*, Bureau of Meteorology website, n.d., accessed 2 October 2023.

40 The Institute of Actuaries of Australia, *Home Insurance Affordability Update [PDF 21.1MB]*, August 2023, p 4.

41 The Institute of Actuaries of Australia, *Home Insurance Affordability Update [PDF 21.1MB]*, August 2023, p 4.

42 The Institute of Actuaries of Australia, *Home Insurance Affordability Update [PDF 21.1MB]*, August 2023, p 4.

43 CHOICE and others, *Weathering the storm: Insurance in a changing climate*, August 2023, p 4.

44 CHOICE and others, *Weathering the storm: Insurance in a changing climate*, August 2023, p 4; see also Insurance Australia Group and Rhelm, *Planned Relocation – Protecting Our Communities,* 28 March 2023; CHOICE and others, *Weathering the storm: Insurance in a changing climate*, August 2023.

The Australian Consumers Insurance Lobby's first evaluation of the pool, published in September 2023, gave the pool a 'needs improvement' verdict.[45] The report also discussed, among other issues facing northern Australian insurance consumers, the consumer impacts relating to marine insurance, including 'escalating premiums' and high cyclone excesses.[46]

The Climate Council conducted a national poll and community survey in December 2022, and found that one in 5 people reported having no insurance and that 6% of those surveyed said they had cancelled their insurance coverage due to the increase in their premiums.[47]

A further concern reported by stakeholders was the need for insurers to reflect any private, property-level mitigation and risk reduction measures by homeowners and owners' corporations in insurance premiums.[48] For example, CHOICE reported that while 44% of surveyed policyholders would consider investing in home mitigation measures to lower the cost of their premium, people are reportedly not being offered lower premiums for undertaking property-level mitigation.[49] The incorporation of the ARPC's mitigation rating factors into insurers' systems is discussed in Section 5.6.

Many stakeholders and advocates continue to advocate for additional public policy responses, or changes to the pool, to address insurance affordability and availability challenges in a changing climate. Some of these proposals are consistent with recommendations we made in the NAII final report:

- **Implementing direct subsidies to address immediate affordability pressures** – The NAII final report recommended that, if governments want to provide immediate relief to consumers facing acute affordability pressures, they should consider direct subsidies over other measures.[50] Since our first report, stakeholders including the Australian Consumers Insurance Lobby and CHOICE have continued to call on governments to consider the use of targeted subsidies in the shorter term.[51]
- **Removing, or rebasing, stamp duties** – The NAII final report recommended that the governments of Western Australia, the Northern Territory and Queensland should abolish stamp duties on home, contents and strata insurance.[52] Alternatively, if stamp duties on insurance remain, they should be re-based with reference to the sum insured value, rather than the premium amount, with a portion of revenue directed towards measures to improve affordability for low-income consumers or to fund mitigation works.[53] Since our first monitoring report, stakeholders have continued to raise the need for reform of taxes and stamp duty on insurance, including the Australian Consumers Insurance Lobby, Actuaries Institute, and the Phase 3 report

45 Australian Consumers Insurance Lobby, *Under the Lens: ACIL's first evaluation of the cyclone and cyclone-related flood reinsurance pool*, September 2023, p 2.

46 Australian Consumers Insurance Lobby, *Under the Lens: ACIL's first evaluation of the cyclone and cyclone-related flood reinsurance pool*, September 2023, pp 6–7.

47 The Climate Council, *Climate Trauma: The growing toll of climate change on the mental health of Australians*, 28 February 2023, p 11.

48 CHOICE and others, *Weathering the storm: Insurance in a changing climate*, August 2023, p 28–9; John Trowbridge, Independent Review of Strata Insurance Practices, *Phase 3: Energising the strata insurance market: A blueprint for affordability, availability, competition*, May 2023, p 22.

49 CHOICE and others, *Weathering the storm: Insurance in a changing climate*, August 2023, p 5.

50 ACCC, *NAII final report*, p xxiv.

51 Australian Consumers Insurance Lobby, *Under the lens: ACIL's first evaluation of the cyclone and cyclone-related flood reinsurance pool*, September 2023, p 5; CHOICE and others, *Weathering the storm: Insurance in a changing climate*, August 2023, pp 7 and 19.

52 ACCC, *NAII final report*, Rec 3.1, p xxiii.

53 ACCC, *NAII final report*, Rec 3.2, p xxiv.

of the Independent Review of Stata Insurance Practices.[54] The current impact of stamp duties and taxes on insurance premiums is discussed in Section 7.2.1 (home insurance), Section 8.2.1 (strata) and Section 9.3.1 (small business).

Insurers' systems and processes

Insurers' internal systems, processes and practices have also been examined in the last year, with the insurance conduct regulator, the Australian Securities and Investments Commission (ASIC), releasing 2 reports on claims handling and pricing practices.

Following a disaster, people want their insurer to handle their claim quickly and fairly. In August 2023, ASIC released its review of home insurance claims handling, calling on insurers to improve their practices and resourcing for claims handling.[55] ASIC reviewed data from more than 218,000 home building and/or contents insurance claims lodged between January and March 2022 from 6 insurers that cover 63% of the Australian home insurance market.[56] Of these claims, 43% related to severe weather events.[57] ASIC identified 5 areas for improvement:

- communication with consumers about decisions, delays and complications
- project management and oversight of third parties
- recognition and management of complaints
- identification and treatment of vulnerable consumers
- resourcing of claims handling and dispute resolution functions.[58]

As discussed below at Section 2.3.1, claims costs from recent catastrophic flooding can contribute to increasing insurance premiums. However, ASIC noted that insurers should be prepared for the 'new normal' of more frequent severe weather events and that the areas for improvement are within insurers' control.[59]

ASIC has also focussed on insurers' internal systems, particularly in relation to pricing. Chapter 4 discusses how insurers set prices, and Chapter 5 discusses insurers' approaches to adapting their pricing systems ahead of joining the pool.

Following previous work that raised concerns about consumer harm from pricing misconduct, ASIC required 11 general insurers, collectively representing 65% of market, to review any potential or actual inconsistency between the pricing promises made to consumers and the promises delivered.[60] ASIC's report, published in June 2023, found 'significant failings' to deliver on the price discounts, benefits or rewards promised by insurers.[61] ASIC found:

- more than 5.6 million consumers were overcharged an estimated $815 million on more than 6.5 million insurance policies

54 Australian Consumers Insurance Lobby, *Under the lens: ACIL's first evaluation of the cyclone and cyclone-related flood reinsurance pool*, September 2023, p 5; The Institute of Actuaries of Australia, *Funding for flood costs: Affordability, availability and public policy options [PDF 1286KB]*, August 2023, p 5; John Trowbridge, Independent Review of Strata Insurance Practices, *Phase 3: Energising the strata insurance market: A blueprint for affordability, availability, competition*, May 2023, p 58. In September 2023, the Tasmanian Government released a draft Bill that proposed abolishing the business services levy: Felix Ellis, Minister for Police, Fire and Emergency Management, *Securing the future of our Fire and Emergency Services*, [media release], 28 September 2023. In November 2023, the NSW government proposed removing the emergency services levy from insurance bills in future: Australian Government, The Treasury, *Government welcomes NSW insurance price reforms* [media release], 16 November 2023, accessed 29 November 2023.

55 ASIC, *ASIC review finds insurers can and should improve claims handling* [media release], 16 August 2023.

56 ASIC, *Report 768*, *Navigating the storm: ASIC's review of home insurance claims* (Report 768), August 2023, p 4.

57 ASIC, *Report 768*, p 5.

58 ASIC, *Report 768*, p 6.

59 ASIC, *Report 768*, p 8.

60 ASIC, *Report 765*, *When the price is not right: Making good on insurance pricing promises* (Report 765), June 2023, p 3.

61 ASIC, *Report 765*, p 3.

- not all participating insurers had 'adequate product governance, systems, processes and controls in place to deliver on their pricing promises'
- ongoing underinvestment in systems, processes and data
- complexity in design and delivery exacerbated the risk of pricing misconduct.[62]

ASIC identified various ways in which insurers were failing to meet pricing promises. For example, the use of pricing constraints which result in a price floor, such as cupping and minimum premiums, can interfere with promised discounts being provided in full. Insurers are expected to return more than $379 million to consumers due to pricing misconduct from the use of price floors – nearly half of the total expected remediation.[63]

As a result of ASIC's review, insurers have committed to refund over $815 million to impacted customers and to fix the identified failings.[64] In June this year, ASIC's civil penalty proceedings against Insurance Australia Limited (IAL) resulted in the Federal Court imposing a $40 million penalty on IAL for pricing discount failures related to a cupping mechanism.[65] ASIC has also commenced civil penalty proceedings against RACQ Insurance Limited for alleged pricing discount failures.[66]

2.2.2 Government and parliamentary processes

Governments and parliaments continue to consider the complex issues impacting insurance consumers in several ways. The ACCC has engaged with, and will continue to engage with government agencies responsible for these related policy developments, and relevant parliamentary inquiries, as our monitoring role continues. This will include engagement both in relation to the substantive outcomes of these initiatives, as well as the data collection processes under the various programs.

Disaster resilience and preparedness programs

There are a range of programs and partnerships focussed on disaster resilience and recovery, generally with the aims of reducing risks from extreme weather events and reducing insurance premiums.

The Hazards Insurance Partnership is a partnership between the Australian Government and the insurance industry, managed by the National Emergency Management Agency. Under the partnership's terms of reference, the Australian Government and insurers commit to work together with the aim of addressing insurance affordability and availability issues as driven by natural hazard risk, to reduce risk for communities and improve Australia's resilience to natural hazards.[67] The ACCC has observer status on the Hazard Insurance Partnership and is a member of its technical working group on data. The National Emergency Management Agency, together with the Commonwealth Treasury and the Australian Climate Service, also committed to 5 strategic insurance projects, including:

- developing a national private mitigation measure knowledge base
- exploring options for public-private partnerships

62 ASIC, *Report 765*, pp 2–3.

63 ASIC, *Report 765*, pp 16–17.

64 ASIC, *Report 765*, p 3.

65 *Australian Securities and Investments Commission v Insurance Australia Limited* [2023] FCA 724; ASIC, *IAL penalised $40 million over pricing discount failures* [media release], ASIC website, 30 June 2023, accessed 15 November 2023.

66 ASIC, *ASIC sues RACQ over alleged pricing discount failures, urges industry to improve pricing practices* [media release], ASIC website, 24 February 2023, accessed 15 November 2023.

67 Australian Government, *Hazard Insurance Partnership – Terms of Reference* [PDF 56.7KB], n.d., [1.1].

- creating an enduring data asset of insurance affordability and underinsurance to inform policy and programs
- reviewing the standard cover regime and various standard definitions.[68]

The Australian Government announced $236 million in funding over 10 years to improve flood forecasting and warnings in the May 2023 budget. Work in Queensland will be prioritised, based on advice from the Bureau of Metrology, due to the high flood risk.[69]

In June 2023, the Australian Government's Disaster Ready Fund (previously named the Emergency Response Fund) announced successful projects from the first round of funding.[70] The fund will provide up to $200 million per year for 5 years to fund community-level disaster resilience and risk reduction, by investing in projects such as flood levees, sea walls, cyclone shelters, evacuation centres, fire breaks and improvements in telecommunications, from 2023–24 onwards.[71]

Programs to raise, retrofit or buyback homes have been established in Queensland and New South Wales, co-funded by state and Commonwealth governments. In Queensland, over 5,550 homeowners have registered for the Resilient Homes Fund with more than 4,100 home assessments completed as at January 2023.[72] Over 130 homeowners have accepted a voluntary buy-back, with others opting for a home raising or retrofit.[73] In New South Wales, the Northern Rivers Reconstruction Corporation released new flood mapping and analysis in June 2023 to support the prioritisation of home buybacks, home raising and retrofits under the Resilient Homes Program.[74] The program will prioritise homes for buybacks in areas that pose the greatest risk to life.[75]

First report of the Joint Select Committee on Northern Australia's inquiry into the pool

Following a referral in October 2022 from the Assistant Treasurer and Minister for Financial Services, the Hon Stephen Jones MP, the Joint Select Committee on Northern Australia commenced an inquiry into the operation and implementation of the pool.[76] The committee released its first report in March 2023, detailing community and stakeholder concerns and expectations about the pool.[77] The report made 7 recommendations designed to address the committee's concerns and improve the implementation of the pool.

However, the committee did not recommend fundamental changes to the design of the pool at that time, noting it was too early to determine whether the pool was fit-for-purpose and meeting its policy objectives given it was not yet fully implemented.[78]

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68 Australian Government, NEMA, *Hazards Insurance Partnership*, NEMA website, n.d., accessed 7 September 2023.

69 Australian Government, *Building a reliable national flood warning infrastructure network* [media release], Australian Government, 15 May 2023, accessed 7 September 2023.

70 Australian Government, National Emergency Management Agency, *Disaster Ready Fund – Round One 2023–24*, accessed 18 July 2023. Cyclone related projects include a severe wind strata study for the City of the Gold Coast and various cyclone shelters for communities in Queensland.

71 Australian Government, Department of Finance, *Disaster Ready Fund*, 29 March 2023, accessed 6 September 2023.

72 Queensland Government, *More than 130 flood-impacted homeowners accept property buy-back offers* [media release], 4 January 2023, accessed 18 July 2023.

73 Queensland Government, *More than 130 flood-impacted homeowners accept property buy-back offers* [media release], 4 January 2023, accessed 18 July 2023.

74 Department of Regional NSW, Northern Rivers Reconstruction Corporation, *Flood mapping and analysis released to support NRRC's buyback priorities*, [media release], NSW Government, 13 June 2023, accessed 18 July 2023.

75 Resilient Homes Program, *Resilient Homes Program frequently asked questions*, accessed 18 July 2023.

76 Parliament of Australia, Joint Select Committee on Northern Australia, *First Report on the Cyclone Reinsurance Pool*, March 2023.

77 Parliament of Australia, Joint Select Committee on Northern Australia, *First Report on the Cyclone Reinsurance Pool*, March 2023.

78 Parliament of Australia, Joint Select Committee on Northern Australia, *First Report on the Cyclone Reinsurance Pool*, March 2023, p 56.

Parliamentary inquiry into insurer responses to the 2022 floods

In July 2023, the Assistant Treasurer announced a new Commonwealth parliamentary inquiry into insurer responses to the significant flooding events in 2022. When releasing the terms of reference, the Assistant Treasurer stated that the inquiry will be 'consumer focussed – investigating land use planning, affordability of coverage, supply chain issues, labour shortages, claims handling, and dispute resolution processes.'[79] The inquiry will also consider the recommendations of other reviews, including ASIC's claims handling review (discussed above) and the external review of insurers' responses to the 2022 floods commissioned by the Insurance Council of Australia, which was released in October 2023.[80]

Separately, the Interim Report of the Senate Select Committee on Australia's Disaster Resilience, released in September 2023, recommended that the new flood inquiry examine insurance companies' handling of flood payouts.[81] The Senate Select Committee also recommended a separate parliamentary inquiry into land planning with respect to natural disaster resilience.[82]

2.3 Economic and environmental conditions influencing insurance premiums

The main purpose of the pool is to lower insurance premiums for households and small businesses in high cyclone-prone regions by reducing reinsurance costs for insurers. Our role involves evaluating whether any savings generated by the pool are being passed through to policyholders. However, in addition to the pool, there are other external factors simultaneously impacting both the costs to insurers of supplying insurance and the prices facing by consumers. These include recent extreme weather events, rising building costs, and hardening reinsurance markets.

2.3.1 Insurers are seeking to recover losses from record flooding events, pushing up insurance costs

Extreme weather events in recent years have contributed to a significant number of claims and losses in general insurance markets. While there was relatively minimal property damage from tropical cyclones in 2022–23, there was significant flooding in 2022 in Queensland, New South Wales, Victoria and Tasmania.[83]

According to the Insurance Council of Australia:

> 2022 was a record year for insured losses, driven by flooding in Northern New South Wales and South-East Queensland in February-March, in the Hawkesbury-Nepean in July, across three states in October, and in the Central West of New South Wales in November. Those events have so far cost $7.17 billion in insured losses from more than 300,000 claims.
>
> ...

79 The Hon S Jones MP, *Insurance claims handling under the microscope in parliamentary inquiry into insurer responses to the 2022 floods* [media release], Australian Government, 3 August 2023, accessed 24 August 2023.

80 Deloitte, *The new benchmark for catastrophe preparedness in Australia: A review of the insurance industry's response to the 2022 floods in South East Queensland and New South Wales (CAT221)*, October 2023.

81 Parliament of Australia, Senate Select Committee on Australia's Disaster Resilience, *Interim Report*, September 2023, p 1.

82 Parliament of Australia, Senate Select Committee on Australia's Disaster Resilience, *Interim Report*, September 2023, p 1.

83 We acknowledge, however, that declared cyclones did cause damage in 2022–23. Cyclone Ilsa, for example, was reported to cause damage to buildings and a caravan park in Pardoo: Insurance News, *Cyclone Ilsa sets new wind record, misses major towns*, 17 April 2023, accessed 7 September 2023.

> [I]nsured losses across all categories totalled $36.5 billion from 5 million claims – meaning last year one quarter of adult Australians made an insurance claim.'[84]

The 2022 east coast floods are the costliest insured event in Australia to date. The floods are estimated to have resulted in 242,000 claims with insured losses of $5.96 billion, where 90% of these claims had been closed as of June 2023.[85] This placed considerable strain on insurers' claims handling capabilities and on consumers. For example, the Australian Financial Complaints Authority received almost 28,000 general insurance complaints over the 2022–23 year, a 50% increase compared to the previous year, with the top issue being claim delays.[86]

General insurers must hold a certain amount of capital to remain solvent and capable of paying claims, according to prudential standards set by the Australian Prudential Regulation Authority (APRA). Insurance premiums can rise or fall due to changes in policyholders' circumstances, but also if an insurer needs to raise capital to pay claims. If an insurer's costs of doing business increase (such as increasing reinsurance premiums and recovering on claims payouts), they may increase insurance premiums to make up the shortfall.

2.3.2 Global and local supply pressures can contribute to rising premiums via higher building replacement costs

Sums insured have a large impact on insurance premiums. The estimated sum insured for a building is based primarily on the estimated rebuild cost, and building costs are generally higher in northern Australia for a variety of reasons. These include the higher building standards that can apply, the availability of materials and labour, and transport and machinery costs. Rebuild costs directly impact the costs insurers face in settling claims. In the event of a major catastrophe, demand surge can further increase claims costs.[87]

We continue to hear that increases in building material and labour costs are contributing to higher building premiums in Australia. This is, in part, due to global supply chain shortages (attributable to continuing disruptions following COVID-19 and from the war in Ukraine), surges in demand from extreme weather events, and general inflation.[88] For example, the major flooding in parts of Queensland, New South Wales, Victoria and Tasmania in 2022 resulted in a surge of claims from affected consumers. Reduced access to supply materials and skilled labour contributed to the increasing cost of insurance claims as the costs to rebuild were considerably higher than the insured value.[89] Swiss Re estimated that the costs of replacing a damaged home in the flooded areas of Queensland and New South Wales could have risen by more than 20%.[90]

Significant natural disasters such as the 2022 east coast floods not only significantly disrupt local economies, but also have flow on effects to broader regional and national economies, for example due to their impact on markets such as tourism and agriculture.[91]

84 ICA, *Inquiry on insurers' 2022 flood response welcomed* [media release], 19 July 2023, accessed 26 July 2023.

85 ICA, *Catastrophe 221: NSW and South East Queensland Floods*, accessed 28 July 2023.

86 Australian Financial Complaints Authority, *Record 97,000 complaints taken to AFCA in 2022–23* [media release], 31 July 2023, accessed 31 July 2023.

87 ACCC, *NAII final report*, p 32.

88 The Institute of Actuaries of Australia, *Home Insurance Affordability Update [PDF 21.1MB]*, August 2023, p 19.

89 Assistant Treasurer and Minister for Financial Services, The Hon Stephen Jones MP, *Insurance claims handling under the microscope in parliamentary inquiry into insurer responses to the 2022 floods* [media release], Australian Government, 3 August 2023, accessed 15 November 2023.

90 Swiss Re Institute, *Sigma – Natural catastrophes and inflation in 2022: A perfect storm [PDF 976KB]*, January 2023, p 14.

91 Queensland Reconstruction Authority, *The social, financial and economic costs of the 2022 South East Queensland Rainfall and Flooding Event [PDF 6.8 MB]*, June 2023, p 10; Australian Bureau of Statistics, *Weather and natural disaster impacts on the Australian national accounts*, 1 June 2022, accessed 4 August 2023.

This in turn can contribute to inflationary pressures on the price of raw materials, labour, and repair costs. Building inflation then leads to increases to the costs of claims and, by extension, insurance premiums as insurers seek to recover on their losses. Furthermore, higher building and repair costs forces up the adequate level of sum insured faced by a consumer, which if not met, can contribute to underinsurance in the event of a claim.

2.3.3 Global reinsurance market conditions impacting local premiums

Reinsurance can be a significant cost component of premiums. The pool aims to reduce the cyclone reinsurance cost for insurers. While insurers must reinsure eligible cyclone risks with the ARPC, they may still need to purchase reinsurance from private markets to cover cyclone risk not covered by the pool and non-cyclonic risk such as flood or bushfire. When reinsurance premiums rise, insurers are likely to reflect this increase in costs, at least to some extent, in the premiums they charge to policyholders.

In 2023 insurers, reinsurers and insurance brokers have consistently stated that the current global reinsurance market remains hard or is hardening.[92] Several factors have contributed to this current state of the reinsurance market, including increased volatility and severity of losses from natural catastrophes and rising inflation.

Reinsurers operate globally and have been increasing their prices while experiencing large losses, largely due to increased claims from weather-related catastrophes.[93] Global costs from natural disasters in 2022 were approximately US$270 billion, of which US$120 billion were insured losses. In the first half of 2023, Swiss Re Group estimated that the overall insured losses from natural catastrophes was 54% above the 10-year average.[94] For example, Hurricane Ian caused approximately US$60 billion in insured damages, a majority of which affected Florida in the United States of America.[95] The impact on the re/insurance markets in Florida was significant, but also extended globally.[96] Marsh McLennan estimated that the effects of Hurricane Ian would contribute to a global shortfall of US$25–50 billion in reinsurer capacity in 2023.[97]

Given these market conditions, some reinsurers have considered it necessary to hold a higher level of capital to cover losses from all perils, not just cyclone, and increase the reinsurance prices they charge to insurers.[98] Several insurers have publicly detailed significant cost increases in their

92 Suncorp, *FY24 Reinsurance Program update [PDF 231KB]*, 4 July 2023, accessed 12 July 2023, p 1; IAG, *Investor Report HY23 [PDF 848KB]*, 13 February 2023, accessed 18 July 2023, p 9; Gallagher Re, *Gallagher Re 1st View: Changing Environment*, 1 July 2022, p 2; Aon, *ILS Annual Report 2022 – Alternative Capital: Growing Markets [PDF 1,131KB]*, accessed 18 July 2023, p 6; Hannover Re, *Hannover Re anticipates improved global reinsurance market terms and conditions to reflect rising loss costs*, 11 September 2023, accessed 9 October 2023.

93 KPMG, *Rising premium prices spark 5-year high insurance sector profit* [media release], 29 March 2023, accessed 15 November 2023.

94 Swiss Re Group, *Severe thunderstorms account for up to 70% of all insured natural catastrophe losses in first half of 2023, Swiss Re Institute estimates*, Swiss Re website, 9 August 2023, accessed 25 October 2023.

95 Munich Re, *Climate change and La Nina driving losses: the natural disaster figures for 2022*, 10 January 2023, accessed 10 July 2023.

96 Swiss Re Institute, *Economic insights: Hurricane Ian to add pressure in an already hardening re/insurance market [PDF 148 KB]*, 2022, accessed 21 August 2023.

97 Marsh McLennan Agency, *Hurricane Ian's impact on the 2023 property market and what that means for your business*, 9 February 2023, accessed 21 August 2023.

98 Australian Financial Review, *The insurance that is too expensive, even for Suncorp*, 4 July 2023, accessed 17 October 2023; Reinsurance News, *Capacity stable at Australia & NZ mid-year renewals as insurers adjust to higher retentions: Aon*, 30 June 2023, accessed 17 October; Reinsurance News, *IAG maintains $10bn cat reinsurance but increases first event retention*, 9 January 2023, accessed 17 October 2023; Insurance Business Mag, *S&P expects premiums to continue rising*, 9 August 2023, accessed 17 October 2023.

reinsurance programs in 2022–23.[99] Some insurers have then responded to increasing reinsurance premiums by passing on these higher costs to consumers via higher insurance premiums.

Insurers can also address these higher reinsurance costs by amending their reinsurance programs and the types of risks they choose to buy cover for.[100] For example, Suncorp dropped a specialised type of disaster cover from its 2023–24 reinsurance program as it considered the costs of reinsuring that cover outweighed the benefits.[101] In another example, IAG chose to take on more of the upfront cost in the event catastrophes occur.[102] In this approach, IAG retains more risk as a way to try and minimise the impact of higher reinsurance costs on its customers.

99 Suncorp, *FY24 Reinsurance Program update [PDF 231KB]*, 4 July 2023 accessed 12 July 2023, p 2; Australian Financial Review, *IAG feels sting of reinsurance disaster pressure*, 9 January 2023, accessed 14 July 2023.

100 Aon, *Reinsurance Market Dynamics June and July 2023 [PDF 749KB]*, July 2023, p 13.

101 Suncorp Group Limited, *FY24 Reinsurance Program update [PDF 223 KB]*, 4 July 2023, accessed 21 August 2023.

102 IAG, *IAG confirms 2023 reinsurance program and 10% quota share renewals*, 10 January 2023, accessed 21 July 2023.

Box 2.1: Insurers recently exiting the California market in the United States of America

The California Department of Insurance states that the insurance market in California is one of the largest in the world, valued at well over US$123 billion.[103]

Various sources say that insurers have exited the market or applied new underwriting guidelines to limit their exposure for some insurance products, largely due to costs associated with natural disasters including wildfire.[104]

American International Group exited the homeowners market in January 2022.[105] More recently, large insurance companies State Farm and Allstate announced that they will no longer provide home insurance to customers in California, effective from May and June 2023, respectively. State Farm stated it made this decision due to 'historic increases in construction costs outpacing inflation, rapidly growing catastrophe exposure, and a challenging reinsurance market'.[106]

From 3 July 2023, Farmers Insurance began limiting its sales of homeowners policies in California, citing 'record-breaking inflation, severe weather events, and reconstruction costs continuing to climb'.[107] This follows Nationwide applying underwriting restrictions to limit their exposure for some products in certain states effective from 14 June 2023.[108]

In September 2023, California's Insurance Commissioner announced various reforms in an effort to improve insurance choices, increase capacity and address the long-term sustainability of the Californian insurance market.[109] Reforms include requiring insurers to write a minimum of 85% of their California market share in high wildfire risk areas and mandating insurance companies to recognize and reward wildfire safety and mitigation efforts. In exchange, insurers will be allowed to use forward-looking catastrophe modelling when they set their rates, which is said will more accurately reflect and price for climate risk.[110]

103 California Department of Insurance, *Insurers Overview*, accessed 4 September 2023.

104 RSM, *California wildfires and Atlantic hurricanes: insurers grapple with rising risk*, 11 August 2023, accessed 2 October 2023; Bankrate, *Limited home insurance options in California as major carriers pull back*, 28 September 2023, accessed 2 October 2023; NPR, *How climate change could cause a home insurance meltdown*, 22 July 2023, accessed 2 October 2023.

105 S&P Global, *AIG to exit California homeowners insurance market at January-end*, 25 January 2022, accessed 4 September 2023.

106 State Farm General Insurance Company, *California New Business Update* [media release], 26 May 2023, accessed 4 September 2023.

107 Forbes, *Farmers Limits Future Insurance Policies in California and Florida. Here's What Homeowners Can Do*, 12 July 2023.

108 Nationwide Mutual Insurance Company, *Nationwide Property & Casualty business actions update*, 12 June 2023, accessed 4 September 2023.

109 California Department of Insurance, *Commissioner Lara announces Sustainable Insurance Strategy to improve state's market conditions for consumers*, [media release], Californian government, 21 September 2023, accessed 5 October 2023.

110 Financial Times, *The insurance world is flirting with its climate doom loop*, 11 October 2023, accessed 19 October 2023; Politico, *California insurance commissioner announces agreement on wildfire coverage*, 21 September 2023, accessed 19 October 2023.

2.3.4 Insurer profitability announcements

Insurers' profits can fluctuate significantly from year to year. As discussed above, insurers have publicly commented that a range of external economic and environmental factors (including extreme weather events, rising building costs and a hardening reinsurance market) have contributed to an increased cost of supplying insurance and increased premiums.

However, despite rising costs, many insurers' 2023 profitability announcements showed strong profits across their general insurance portfolio as a whole.[111] Some example announcements include:

- IAG reported a 37% increase in insurance profit (up to $803 million).[112]
- Suncorp reported a 334% increase in profit ($174 million to $755 million) for its Insurance Australia brand.[113]
- QBE reported a 733% increase in profit ($48 million USD to $400 million USD).[114]
- Youi reported an increase in operating profit of 216% (from $57 million to $117 million).[115]

Overall, APRA reported that the insurance industry reported a net profit after tax of $4.6 billion and a return of investment on net assets of 14% for the year ending 30 June 2023.[116]

Whilst some commentators have linked higher premiums to higher profits, others have noted that a range of other factors contributed to higher profits, such as a turnaround from losses in investment markets a year ago and the release of funds previously set aside for pandemic-related business claims that did not eventuate.[117] Additionally, several insurers note that while they recorded profit in Australia in 2022–23 due to lower catastrophe losses, they recorded significant losses in New Zealand.[118]

In Chapter 10 we report on the insurer profitability data that we have collected, with a particular focus on home and strata insurance in northern Australia. Chapter 10 notes that while northern Australia has seen an improvement in profitability in 2022–23, profits are generally volatile and can vary from year to year depending on cyclical market conditions (including inflation, construction cost, labour costs, regulatory requirements and catastrophic events).

111 General insurance covers a range of personal and commercial classes of insurance including home, strata, travel, motor, consumer credit, business liability and industrial special risks. General insurance does not include classes of life insurance; Tasman Asia Pacific, *General Insurance Code of Practice [PDF 84.6KB]*, n.d., accessed 27 November 2023..

112 IAG, *IAG announces FY23 results [PDF 466KB]*, 21 August 2023, accessed 3 October 2023.

113 Suncorp, *Suncorp Full Year 2023 Results*, 9 August 2023, accessed 3 October 2023.

114 QBE, *Market Release for the half year ended 30 June 2023 [PDF 1,816KB],* 10 August 2023, accessed 3 October 2023.

115 OUTsuance Group Limited, *Integrated Report 2023 [PDF 13.3MB]*, accessed 4 October 2023.

116 APRA, *APRA releases general insurance statistics for June 2023*, 24 August 2023, accessed 4 October 2023.

117 Australian Financial Review, *More premium pain coming but customers sticking with cover, IAG says*, 21 August 2023, accessed 4 October 2023.

118 Suncorp, *Suncorp Full Year 2023 Results*, 9 August 2023, accessed 3 October 2023; Australian Financial Review, *Insurers rung hot as investors chase rising premiums,* 10 August 2023, accessed 4 October 2023.

3. Insurer participation in the pool

In this chapter, we briefly examine current participation in the pool by insurers and factors influencing insurers' decisions on timing of entry to the pool, including implementation issues and challenges.

In Section 3.1, we outline the insurers that are participating in the pool as at November 2023. While the pool has been operational since 1 July 2022, the first insurers did not join until the start of 2023, when 2 insurers joined, and it was then a further 6 months until other insurers also joined. Currently, there are 11 insurers that have joined the pool.[119] Entry so far indicates that insurers are using different approaches to transition eligible policies into the pool (for example, bulk transfers or progressive transfers). Alongside the timing of insurer entry, we also note other events relevant to the operation of the pool, and note the different legislative deadlines for large and small insurers.

In Section 3.2, we discuss the considerations influencing insurers' timing of entry to the pool, and implementation of changes to systems and processes needed to operationalise the pool. Overall, we found that the private reinsurance renewal period appears to be the most notable factor influencing the timing of insurer entry. We also outline the main implementation issues and challenges that insurers have raised in relation to joining the pool. Some of these are consistent with issues raised by insurers that we reported on last year, particularly in relation to the claims period. Overall, however, concerns appear to have largely shifted from anticipated administrative challenges to actual implementation considerations, including:

- updating peril modelling
- the need to quantify any 'gap' in coverage for cyclone losses incurred outside of the defined claims period
- administrative and systems changes to implement the pool.

119 Allianz (Allianz Australia Insurance Ltd), Sure (representing Liberty Mutual Insurance Company, Pacific International Insurance, and The New India Assurance Co Ltd), QBE (QBE Insurance (Australia) Ltd), Suncorp (AAI Limited), Hollard (both Hollard Insurance Partners Limited and The Hollard Insurance Company Pty Ltd), RAC (RAC Insurance Pty Limited), RACQ (RACQ Insurance Limited), Youi (Youi Pty Ltd), RAA (RAA Insurance Limited), Auto & General (Auto & General Insurance Company Limited), IAG (Insurance Australia Group Limited): ARPC, *Cyclone pool insurer customer listing*, ARPC website, accessed 17 November 2023.

3.1 Current participation in the pool

Since the pool commenced operation on 1 July 2022, the ARPC has revised its pool premium rates in October 2022, and subsequently entered reinsurance agreements with insurers as they joined the pool.[120] The ARPC has also declared 4 cyclone events on the advice of the Bureau of Meteorology.[121] Figure 3.1 below sets out a timeline of the notable developments relating to the pool and highlights which insurers have joined the pool. It can be seen that Allianz and Sure were the first insurers to join the pool in January 2023, while another group of 7 insurers joined around June/July 2023.[122] An additional 2 insurers had joined by November 2023.[123]

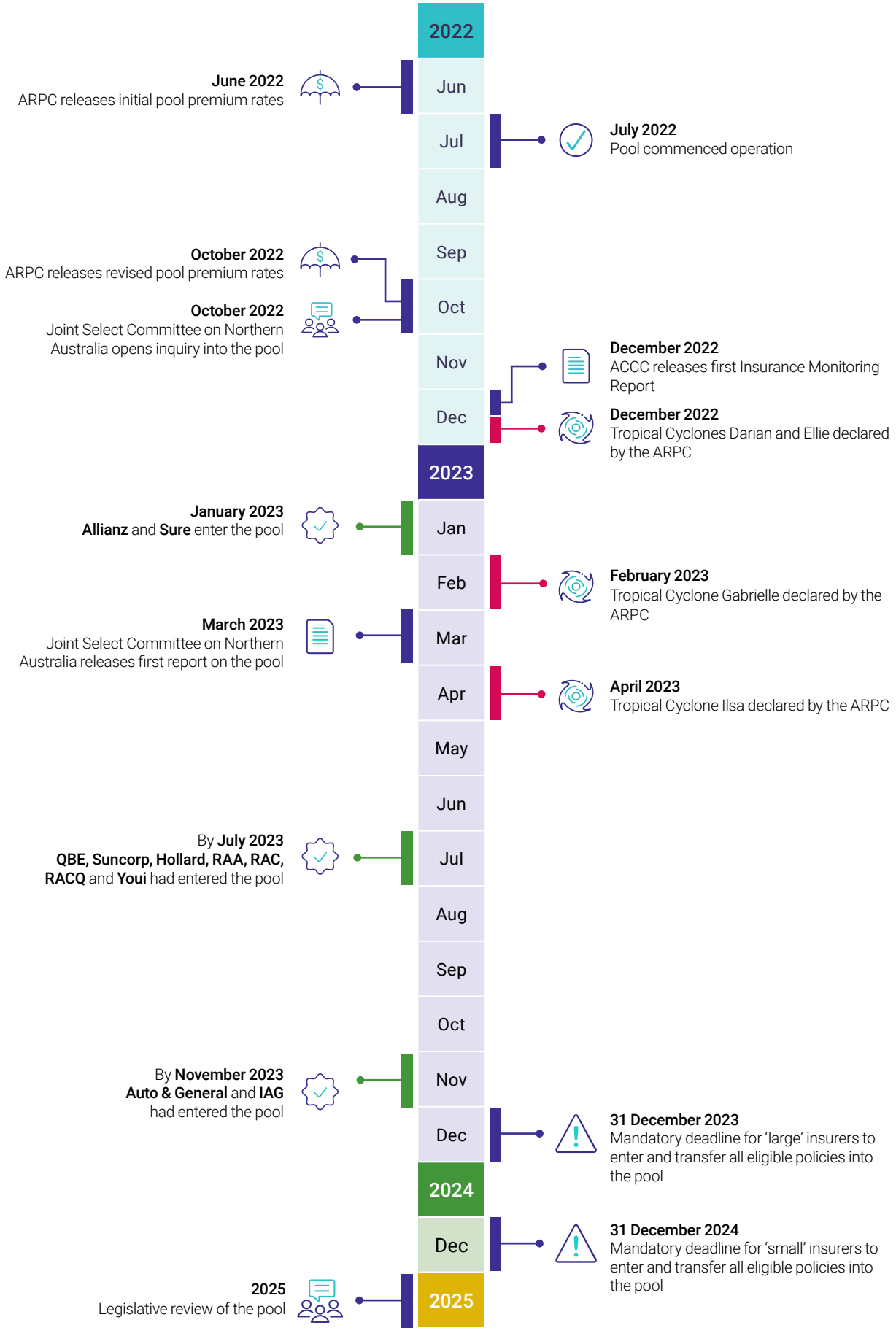
120 ARPC, ARPC – *Premium Rate Assessment Report Update for Consultation – 1 October 2022*, ARPC website, accessed 27 September 2023; ARPC, *Cyclone pool insurer customer listing*, ARPC website, n.d., accessed 3 November 2023.

121 ARPC, *Declarations – Cyclone declarations*, ARPC website, n.d., accessed 26 August 2023.

122 ARPC, *ARPC welcomes Allianz to the Cyclone Reinsurance Pool* [media release], ARPC, 13 January 2023, accessed 23 October 2023; ARPC, *ARPC welcomes Sure Insurance to the Cyclone Reinsurance Pool* [media release], ARPC, 18 January 2023, accessed 23 October 2023; Sure, *Sure Insurance – Participation In Federal Government Cyclone Reinsurance Pool* [media release], Sure, 18 January 2023, accessed 23 October 2023; Allianz, *Allianz Direct Home Insurance now available in new areas across Northern QLD and WA, after joining the Cyclone Reinsurance Pool* [media release], 1 March 2023, accessed 1 November 2023; Allianz, *Allianz joins the Cyclone Reinsurance Pool* [media release], Allianz, 16 March 2023, accessed 6 October 2023; RACQ Insurance, *News: RACQ Insurance joins Cyclone Reinsurance Pool*, 3 July 2023, RACQ Insurance website, accessed 1 November 2023; Suncorp, *News*: *Suncorp joins Cyclone Reinsurance Pool*, 30 June 2023, Suncorp website, accessed 1 November 2023; QBE, *The Cyclone Reinsurance Pool explained – what's changing and why* [media release], QBE, 27 July 2023, accessed 6 October 2023; InsuranceNews.com.au, *Government talks up cyclone pool as QBE and other insurers join*, 14 July 2023, InsuranceNews website, accessed 1 November 2023; ARPC, *ARPC Annual Report 2022–23*, 20 September 2023, p 60; ARPC, *Cyclone pool insurer customer listing*, ARPC website, accessed 1 August 2023.

123 ARPC, *ARPC Annual Report 2022–23*, 20 September 2023, p 60; ARPC, *Cyclone pool insurer customer listing*, ARPC website, accessed 17 November 2023; IAG, *IAG joins Cyclone Reinsurance Pool* [media release], IAG, 13 November 2023, accessed 13 November 2023.

Figure 3.1: Timeline of pool development and events



As part of the pool design, insurers can choose how to transfer their portfolios into the pool. For example, insurers may choose a single bulk transfer of all eligible policies or transfer by a progressive approach, whereby certain classes of eligible policies, or certain brands, are transferred at different times, as long as all eligible policies are transferred on or before the mandatory deadline. For example, Allianz has already transitioned its household policies (home building, home contents, and landlord) and has indicated it will transfer eligible strata and SME policies by the mandatory deadline.[124] Allianz has made a public statement that its participation in the pool from 1 January 2023 enabled it to 'expand the sale of household insurance directly to customers in northern Queensland and Western Australia' (see Section 6.3 for further discussion on the availability of insurance).[125] As another example, QBE has similarly indicated it is taking a progressive approach, by entering the pool and transferring some eligible policies and working towards transitioning the remaining eligible policies before 31 December 2023.[126] In comparison, Suncorp indicated that, from entry, all eligible customers at the point of renewal and any new business policies for home, strata, landlord and small business property insurance across the Suncorp's brands could access the pool.[127]

As set out in Chapter 1, general insurers are required to reinsure all their eligible cyclone risks with the ARPC by their respective legislated deadlines. As such, we expect more insurers to join the pool over the course of our monitoring in 2024, noting the deadline for small insurers is 31 December 2024. Additionally, we note some insurers are not required to participate in the pool but can choose to do so.[128]

The requirement on large insurers to transfer all of their eligible policies by the end of 2023 has meant that providers of the bulk of Australian insurance policies had joined the pool by the time of this ACCC report. In July 2023, the ARPC stated that it expected, by the following dates, the proportion of Australian home insurance policies covered by the pool to be:

- 65% of home insurance policies from 1 July 2023
- 95% of home insurance policies from 1 November 2023 (when the 2023–24 cyclone season begins).[129]

While there are 11 insurers currently participating in the pool, this is not indicative of the number of insurers offering insurance in all regions, particularly in northern Australia. Some of these providers will not supply any significant number of policies in northern Australia generally or will only supply to a limited set of regions. Chapter 6 examines insurers' presence in cyclone-prone regions and explores how the pool might influence the availability of insurance in those regions.

3.2 Insurers' considerations on timing of entry and implementation

In 2022, most insurers considered themselves on track to join the pool by their relevant legislative deadlines, however many found it difficult to decide on a conclusive implementation plan.[130] Common challenges raised by insurers in relation to pool implementation and the timing of entry that were detailed in our first report included access to information about the pool (mainly relating to the

124 Allianz, *Allianz joins the Cyclone Reinsurance Pool* [media release], Allianz, 16 March 2023, accessed 6 October 2023.

125 Allianz, *Allianz Direct Home Insurance now available in new areas across Northern QLD and WA, after joining the Cyclone Reinsurance Pool* [media release], Allianz, 1 March 2023, accessed 11 September 2023.

126 QBE, *The Cyclone Reinsurance Pool explained – what's changing and why* [media release], QBE, 27 July 2023, accessed 6 October 2023.

127 Suncorp, *Suncorp joins Cyclone Reinsurance Pool*, [media release] 30 June 2023, accessed 30 October 2023.

128 Australian Government, *Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Bill 2022*, Schedule 1, items 5, 7 and 9, section 3 and subsections 8A(5), 8A(6), 8A(9) and 8A(10) of the *Terrorism and Cyclone Insurance Act 2003*.

129 ARPC, *Update on the new financial year for the cyclone pool*, ARPC Website, 6 July 2023, accessed 28 August 2023.

130 ACCC, *Insurance monitoring report 2022*, (First insurance monitoring report), 20 December 2022, p 47.

release of the ARPC premium rates), required administrative and system changes, and the timing of private reinsurance agreement negotiations.[131]

Since our first report, the ARPC has continued to work with insurers to support their transition into the pool, including 'small' insurers that are in earlier stages of planning in relation to the pool. Overall, insurers' considerations about the timing of their entry into the pool vary and relate to their approach to implementing the pool into their systems. The timing of private reinsurance renewals remains a major consideration for insurers' timing of entry to the pool. Smaller insurers have indicated they remain in the early stages of planning and continue to make required adjustments to internal processes and systems in preparation for transitioning to the pool. However, they expect to join the pool throughout 2024, aligning with renewal of their private reinsurance agreements. Insurers that have already joined the pool and are currently implementing associated changes arising from the pool into their systems have stated this process came with an array of challenges and considerations before, during and after their entry into the pool, discussed below at 3.2.2 and 3.2.3.

3.2.1 Timing of private reinsurance renewals

Consistent with observations in our first report, information provided by insurers in 2023 indicates that their timing of entry into the pool has largely been dependent on the timing of their existing private reinsurance renewals. Most insurers expressed the need to align entry into the pool with the expiration of their existing private reinsurance agreement. Joining the pool during the term of an insurer's existing reinsurance agreement would result in insurers needing to pay the ARPC premium on top of the existing private reinsurance premium for the same risk, unless a partial refund was agreed with the private reinsurer. For example, one insurer was concerned it would not be afforded any reinsurance premium relief in 2022–23 if it entered the pool progressively over that year. Most insurers had finalised their 2022–23 private reinsurance agreements by the time of the pool's commencement on 1 July 2022. Accordingly, insurers waited until their agreements expired before entering the pool; as highlighted by the bulk entry of insurers in July 2023.

3.2.2 Claims period and peril modelling

Consistent with issues raised in our first report, administrative and system changes are a continuing challenge reported by both large and small insurers, which has been an influence on their considerations on when and how to enter the pool. Those administrative and system changes largely arise because the pool establishes a particular set of parameters for considering cyclone risk that differs to insurers' existing approaches.

As discussed in Section 1.2.1, the pool is legislated to cover eligible losses arising during the claims period for a cyclone event, which lasts from the time a cyclone begins until 48 hours after the cyclone ends. This claims period, sometimes referred to as the '48-hour period', demarcates what is (and is not) covered by the pool. As noted in our first report, many insurers held significant concerns about the claims period, considering that this is a significantly shorter coverage period than the private reinsurance market, which is generally 7 days, no matter the length of the cyclone, with the insurer deciding when that coverage starts.[132]

In documents received in 2023 some insurers remained concerned, pointing to Cyclone Ellie (the claims period for which ran from 22–25 December 2022 and ended prior to later damages occurring in early January 2023) as an example of the gaps relating to the 48-hour claims coverage period that may arise. No insurer had joined the pool at the time that Cyclone Ellie was declared by the

131 ACCC, *First insurance monitoring report*, pp 48–49.

132 ACCC, *First insurance monitoring report*, p 51; Parliament of Australia, Joint Select Committee on Northern Australia, *First Report on the Cyclone Reinsurance Pool*, March 2023, p 47, para 3.64; RACQ, *RACQ submission to Joint Select Committee on Northern Australia inquiry into the Cyclone Reinsurance Pool [PDF 509KB]*, accessed 29 September 2023.

ARPC, so no claims were actually made against the pool.[133] However, some insurers highlighted that the heaviest property damages from the cyclone arose *after* the 48-hour coverage window closed (i.e. after 25 December), particularly in relation to cyclone-related flooding. These insurers believed Cyclone Ellie highlighted the limitations of the pool's coverage under certain event scenarios and that private reinsurance would be required to cover these losses.

Many insurers continue to raise the claims period as a challenge when looking to implement the pool. The coverage that insurers provide to policyholders may include coverage for cyclone-related losses that fall outside the pool's defined claims period, meaning the risk of those losses won't be reinsured with the ARPC. This has resulted in several insurers needing to update their peril modelling to accurately determine what risks fall within the legislation's definition of an 'eligible cyclone loss' (and therefore covered by the pool) and what falls into the 'gap'. For example, one insurer has not previously rated premiums for cyclone as a separate peril and has instead historically modelled expected cyclone costs under the broader banner of 'storm'. To the extent insurers considered there is a coverage 'gap', insurers may then need to determine whether to retain the risk of any losses that fall outside the pool, or to cede those risks to private reinsurance arrangements. For a further discussion on changes to peril modelling, see Section 5.2.1.

3.2.3 Other systems changes

Additionally, insurers will need to update their systems and processes to capture policyholder mitigation data in accordance with the ARPC's reinsurance mitigation discounts, which are summarised in Section 5.1. As detailed in Section 5.6, we have observed differing approaches to insurers' actual implementation of the ARPC's mitigation discounts to date. While insurers initially expressed support for incorporating risk mitigation into the pool's pricing formula, some documents indicated that implementing the mitigation rating factors has not been straightforward.[134]

Some insurers also mentioned other difficulties and costs associated with amending internal systems, such as:

- the need to work through a 3rd party supplier to update peril models
- the level of data and details required to use the ARPC's new 'PACE' portal, through which insurers lodge their reinsurance premium and claims information with the ARPC
- difficulties in replicating the pool formula in internal systems (as an example, due to the application of discounts, capping/cupping, and differences in the information captured by the insurer and information required by the ARPC).[135]

3.2.4 Issues raised by 'small' insurers

On analysis of materials provided by 'small' insurers that are required to join the pool by the end of 2024, most have indicated they are still in the early stages of considering their implementation of the pool and continue to work towards a definitive approach prior to joining. In saying that, they generally have highlighted similar challenges as the larger insurers, namely, aligning reinsurance agreement periods, complexities of system changes needed, and calculating any gap in pool coverage. Some 'small' insurers have expressed that they anticipate utilising the additional 12 months until their mandatory deadline, after the deadline for 'large' insurers, to observe how the 'large' insurers approach entry to the pool and to incorporate any learnings prior to their own entry to the pool.

133 ARPC, *ARPC Annual Report 2022–23*, 20 September 2023, p 15.

134 ACCC, *First insurance monitoring report*, p 56.

135 ARPC, *About PACE*, n.d., accessed 13 September 2023.

4. How insurers set premiums

There are many factors that determine the final retail premium that insurers offer consumers for their insurance policies.[136] In this chapter, we outline how insurers 'build' premiums for products covered by the pool through a process drawing from a number of cost inputs and other factors, including those most directly affected by the pool.

As set out in Section 1.3, we obtained detailed data from insurers showing the premium breakdown for insurance products which fall within the scope of the pool. We also obtained information and internal documents from insurers which explain their approach to premium pricing. We have compared this information to the detailed premium breakdown discussed in the NAII final report[137] and consider that insurers' approaches to building premiums are broadly similar and remain consistent with the findings of that report. This consistency in approach to pricing is significant in that it allows the ACCC to build on its understanding from the data collected during the Northern Australia Insurance Inquiry for this current monitoring task to provide a longitudinal view of prices over time. It also allows us to draw on relevant findings about how insurers build premiums to assist our understanding of the effect of the pool.

In addition, we outline information about insurers' approaches to premium calculation for SME insurance. This product was not examined in the Northern Australia Insurance Inquiry but we find that the steps in pricing are largely consistent with other premium calculation approaches, including for home and strata insurance.

The pool is designed to improve insurance affordability for households and small businesses in cyclone-prone areas by seeking to reduce insurers' reinsurance costs.[138] Reinsurance costs are a significant cost component for insurers, but are only one of several inputs, each of which can influence premiums. We provide a breakdown of cost components for products covered by the pool in Chapters 7 to 9. In Chapter 5, we also discuss insurers' views on the expected impact of the pool on reinsurance costs and premium calculations more broadly.

While the broad approach to pricing is similar, the specific methods used vary significantly between different insurers. Insurers have complex pricing engines, systems, practices and controls in place to build premiums. Some elements of the premium setting process, in particular estimating expected natural peril claims costs, involve a great deal of uncertainty. We found that some insurers have developed systems that allow them to more readily breakdown premium cost components at a detailed level compared to other insurers. Relatedly, some insurers collect data in ways that will enable them to more easily demonstrate the change in premium cost components and impact on premiums arising from the pool. This issue is discussed in more detail in Chapter 5.

Insurers also adjust premiums for a range of reasons, including assessments of competitor pricing and to manage their exposure to particular risks. Considerations about risk selection and availability of insurance are further discussed in Chapter 6.

All of these differences in systems, practices, adjustments and controls between insurers mean that the implementation of the pool will be complicated, and will vary from insurer to insurer, including in their ability to demonstrate the impact of the pool. The differences also mean that it is not always clear how, or whether, final premiums paid by customers reflect the cost of providing the insurance product. This means that there may be a level of opacity caused by these adjustments that will limit customer visibility of pool savings pass-through. These complexities also need to be viewed in the

136 ACCC, *NAII final report*, p 84.

137 ACCC, *NAII final report*, Chapters 4, 7 and 10.

138 ACCC, *First insurance monitoring report*, p 19.

context of the legislative framework for the pool where, as set out in Chapter 1, insurers are not obligated to pass-through any savings from the pool to consumers in a particular way.

4.1 Overview of how insurers calculate premiums

Insurers' pricing methodologies have a number of elements, and each insurer's exact approach differs according to its own preferences and systems, including among brands within the same insurer. However, generally, insurers' approaches to setting premiums can be conceptualised as set out in Figure 4.1.

Figure 4.1: Generalised process diagram for calculating a premium

Insurers first calculate and set a '**technical premium**', which reflects their estimate of the costs of providing insurance with a margin added for profit and/or return on capital (we will refer to this simply as 'margin'). Technical premiums differ across policies, as each policy will contribute to these costs to a different extent depending on the nature of the insured property.

Once the technical premium is calculated, insurers often make '**premium adjustments**'. These adjustments are changes that insurers make in response to other factors not specifically related to the property being insured. Adjustments can be made for a range of reasons, such as competitive or market positioning or to manage their exposure. These changes often reflect the insurers' overall corporate strategies. Insurers may also apply '**discounts**' to their premium calculation. Discounts may be applied for things such as customer loyalty, online purchase, and no claims bonuses.

Insurers then apply '**surcharges, taxes, and duties**', to the adjusted technical premium to arrive at the retail premium. Surcharges may be included for things such as monthly payment options. The insurer will then add any relevant levies, taxes, and duties to give the final retail premium.[139]

The approach described above is a generalisation of the approaches taken by insurers to calculate premiums. We understand that there will be variations in this process across all insurers, and also within each insurer for different products. The variations around process is amplified by the systems that insurers use to price their products. Box 4.1 goes into this in more detail.

139 ACCC, *NAII final report*, p 61.

Box 4.1: Complexity of insurers' pricing engines

The NAII final report notes several insurers were of the view that the complexity of their pricing systems makes it difficult to identify the components of the technical premium, either at an average level across regions, or for individual consumers.[140] It also found evidence in insurers' documents which suggests that it is not always clear within insurers how the assessment of technical premiums is transformed into the final retail premiums.[141]

In information we have obtained from insurers for the purposes of this monitoring report, we have seen evidence of some insurers working to address these issues by multiple avenues, including improving internal capabilities as well as through external software solutions. Internal reporting from some insurers suggests that while they may expend considerable resources on calculating technical premiums which accurately reflect risk, it is not clear that this is always directly reflected in the final retail premium paid by the customer.[142]

4.2 Setting a technical premium

The setting of a technical premium is the first step in the price-setting process outlined in Section 4.1. Setting a technical premium is a multi-stage process and, for expected natural peril claims in particular, involves a great deal of uncertainty.[143] Information we received from insurers indicated that a limited number of insurers operate an end-to-end pricing process at the policy or address level for calculating technical premium components. Generally, many insurers derive technical premiums at the policy or address level by first considering some cost components at an aggregated level (for example, calculating the cost that applies to an entire class or category of insurance products supplied by the insurer, such as home insurance) before allocating the proportional cost component to each policy according to the policy's risk characteristics, exposures to a risk and product type. By initially modelling cost components at an aggregated level, insurers are able to consider factors such as the relative costs of other portfolios and determine an appropriate technical cost for the given portfolio.

As further discussed in Chapter 5, this means that the property-level pricing used to determine ARPC reinsurance premiums may be reflected in technical premiums in a variety of ways by insurers.

Figure 4.2 below illustrates the cost layers that build to the technical premium and the components within each layer.

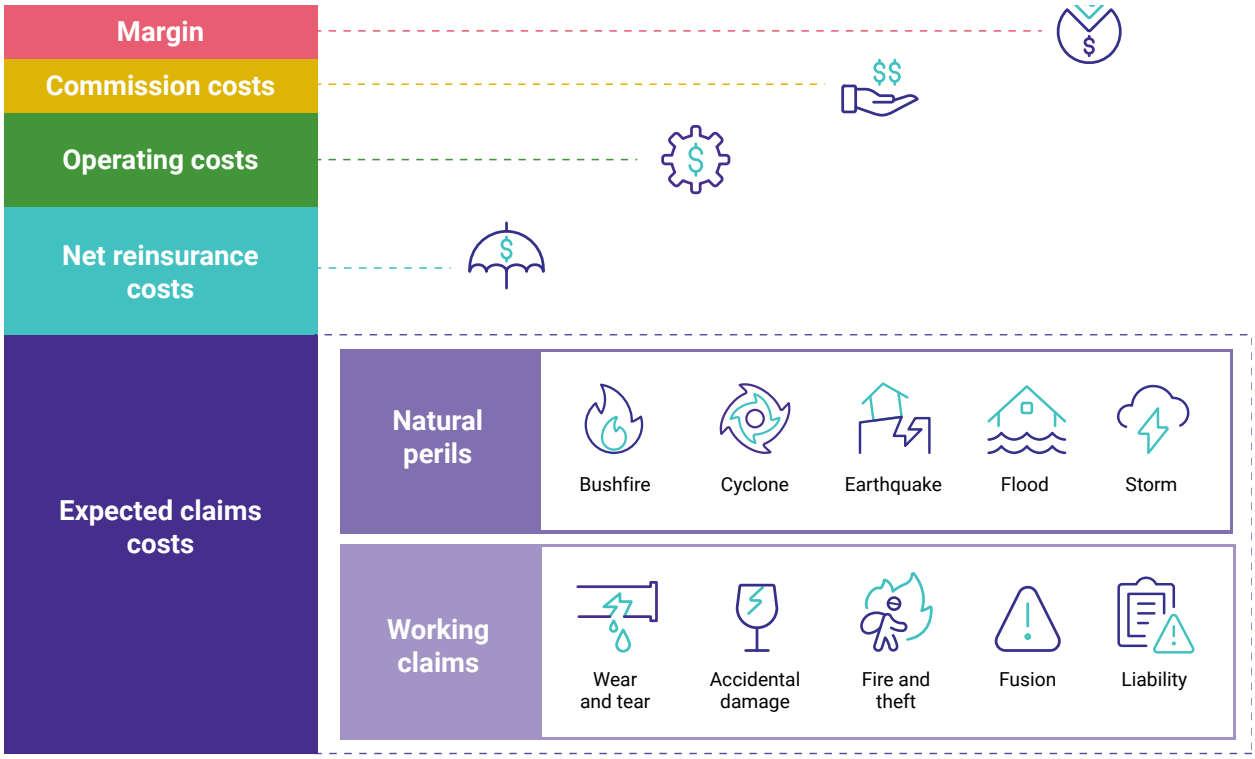
140 ACCC, *NAII final report*, p 83.

141 ACCC, *NAII final report*, p 83.

142 ACCC, *NAII final report*, p 84.

143 ACCC, *NAII final report*, p 61.

Figure 4.2: Technical premium components



Insurers generally calculate each cost component separately (whether at a property or portfolio level), then combine the components to determine the technical premium as detailed below:

- *Expected claims costs*: these are generally split into working claims, and natural peril or catastrophe claims. Working claims are claims that are not caused by a natural peril or catastrophe (for example, accidental damage or theft).
- *Net reinsurance costs*: these are the costs to the insurer of acquiring reinsurance coverage, less expected reinsurance recoveries.
- *Operating costs*: these include administrative expenses, marketing costs and claims handling costs.
- *Commission costs*: these are payments made to an intermediary, where insurance is purchased through a distributor or broker.
- *Margin*: this is the margin added to the technical premium for profit and/or a return on capital. The margin component may also be set with reference to the amount of prudential capital required to support the policy being provided, and this will vary with the risk profile of the policy.[144]

We discuss each of these technical premium components below.

144 ACCC, *NAII final report*, p 61.

4.2.1 Expected claims costs

Expected claims costs are an insurer's estimated costs associated with paying any future claims during a particular policy period. Expected claims costs are the largest cost to insurers and therefore represent the largest part of the technical premium.[145] Calculating the expected claims costs is one of the more complex parts of determining the technical premium, as these costs are uncertain and can be difficult to predict, particularly in relation to pricing natural peril risks.[146] As a result of this, insurers often calculate these costs across the whole portfolio. This ensures enough premiums are collected to cover the expected overall costs before being allocated down to the individual policy according to allocated risk rating factors.

To calculate expected claims costs, insurers generally split claims costs into 2 further categories:

- Natural peril or catastrophe claims: these are claims arising from natural perils, catastrophe events or other significant weather events. They include claims from flood, cyclone, bushfire, earthquake, hail, storm and storm surge. Insurers generally model expected claims for each type of peril separately.[147] Natural peril risks can be significantly more severe when they occur, but generally happen less frequently than working claims.[148]
- Working claims: these are claims that do not relate to natural perils or catastrophes, or other significant weather events. They include claims for things such as fire, theft, glass, and electrical or water damage (excluding from natural peril/catastrophe events). Generally, working claims are easier to model than peril claims as they are less volatile.[149] Overall, insurers' methodologies for determining working claims were broadly consistent. For most insurers, working claims are determined by using internal claims data and experience, and generally external models are not used.[150]

Insurers generally use separate models for calculating the different claims types. While these models differ, they are usually 'frequency and severity' models. That is, the models will calculate the frequency (or the likelihood of the claim type occurring) and the severity (the likely cost of a claim when it occurs) of the claim type for a policy. The frequency and severity outputs are then used to calculate the per policy cost for the claim type, which depends on the characteristics of the particular property and its location.[151] Insurers often use internal claims data and/or external data models with the aim of accurately predicting future claims. One insurer stated that the natural peril component is evaluated as part of its reinsurance treaty renewal as internal claims experiences data is not sufficient to model these perils.

We understand that, for most claim types, the location of the property and the sum insured have the greatest impact on the estimated claims cost.[152]

Natural peril claims modelling

Natural peril claims models are particularly complicated and require a significant amount of data. The models used by insurers to calculate the risk of natural peril claims are generally developed by

145 ACCC, *First insurance monitoring report*, pp 43–47.

146 ACCC, *NAII final report*, p 61.

147 ACCC, *NAII final report*, p 62.

148 Suncorp, *Submission to the ACCC Northern Australia Insurance Inquiry*, Suncorp website, pp 16–17, accessed 15 November 2023.

149 ACCC, *NAII final report*, p 69.

150 ACCC, *NAII final report*, p 62.

151 ACCC, *NAII final report*, p 62.

152 ACCC, *NAII final report*, p 62.

industry specialists and supplemented with insurers' own claims data.[153] A combination of internal and external models are also used to determine the cyclone component of a premium.[154]

Information provided by insurers indicates there is an element of discretion around selecting which models to use, further adding to the complexity of the modelling process. One insurer provided documentation showing that it combines 3 external models for its bushfire risk calculations and, where their risk ratings conflict, the insurer has had to decide which rating it deems the most accurate.

A key development over the past decade has been the increasing sophistication and granularity of natural peril modelling.[155] For example, insurers typically use a variety of rating factors when modelling for cyclone, which can include the proximity of the property to the coast, the slope of the surrounding terrain, building construction factors (such as roof and wall material, and the age of the building), and wind shielding.[156] Relevantly for the pool, a number of insurers assess cyclone premiums at an address level, rather than an average risk at a postcode or larger regional level, which can allow them to make a more accurate assessment of the cyclone risk an individual property faces.

Some insurers detailed how more granular risk modelling has resulted in changes to premiums at a policy level, with some consumers in higher-risk areas seeing premiums increase and others in lower-risk areas paying less for their premiums. One insurer stated that changing its external risk model from one that provided a top-down, CRESTA-zone approach to one that provided a granular, bottom-up approach showed that it had been 'overcharging' for cyclone, and applying its new rate would allow for portfolio growth and diversification in 'very low to low' cyclone risk areas. However, this insurer also noted that this increased granularity would cause some consumers to see price increases.

In Chapter 3 we noted the challenges insurers have expressed in relation to changes to natural peril modelling arising from the pool. We go into further detail about the effect of the pool on natural perils claims modelling in Chapter 5.

Working claims, including their role in SME insurance

As outlined earlier, working claims are essentially non-natural peril claims (or non-catastrophe claims), such as burst pipes, fire, theft, and glass cover.[157] Consistent with findings in the NAII final report, information received from some insurers indicates working claims are determined by using internal claims data and experience, and external models are generally not used.[158] This practice arises primarily because working claims are generally easier to model than natural peril claims as they are less volatile. However, modelling expected claims costs for these types of risks can still be complex.[159] One insurer also identified that because of the relatively stable nature of working claims, competitor and market monitoring plays an influential part in pricing working claims (this is discussed further in Section 4.3.2).

Small business insurance premiums are more heavily influenced by working claim costs and risks over that of natural peril risks. Working claims for small businesses reflect the nature of the business and SME insurance products are tailored accordingly. Information received from some insurers identified that factors such as occupation and the nature of the business operations influence expected claims costs. From the customer perspective, policyholders have the ability to build and

153 ACCC, *NAII final report*, p 62.

154 ACCC, *NAII final report*, p 64.

155 ACCC, *NAII final report*, pp 64 and 67.

156 ACCC, *NAII final report*, p 64.

157 ACCC, *NAII final report*, p 69.

158 ACCC, *NAII final report*, p 69.

159 ACCC, *NAII final report*, p 69.

customise their policies to some extent to suit their needs and circumstances.[160] For example, a commercial kitchen may seek more fire cover owing to its higher fire risk compared to a professional services business. Businesses may also lease the property and therefore are less likely to insure against building damage associated with natural peril risks.[161] Some insurers also noted that calculating and setting sum insured amounts for SME insurance products is commonly left to the policyholder or broker to determine.

Further details about SME insurance products covered under the pool is discussed in Chapter 9.

4.2.2 Reinsurance costs

Once an insurer has calculated its expected claims costs, the next component of a technical premium is reinsurance. Reinsurance is taken out by insurers, generally at a whole of portfolio level, to protect insurers from significant losses impacting their portfolios.[162]

Box 4.2 provides a general overview of reinsurance. For all home and contents insurance, reinsurance cost makes up between 22% and 41% of the cost per policy in all regions in 2022–23. See Section 7.2.2 for more information.[163]

Box 4.2: What is reinsurance?

Reinsurance is effectively insurance for insurers. Insurance works by spreading the cost of risks among a large number of policyholders facing similar risks. Insurers collect (relatively smaller) premiums from their many policyholders and pay out (relatively larger) claims if an insured event occurs. This is how insured risks are mitigated. Similarly, reinsurance is a risk management tool designed to protect insurers from large financial losses when paying out claims to policyholders. In return for transferring risk to reinsurers, insurers pay reinsurance premiums.

The amount of risk that insurers choose to cede to reinsurers and the types of reinsurance they use depends on, amongst other factors, how much capital insurers choose to retain and how significantly they want to diversify their risk. Additionally, insurers are subject to prudential capital requirements under APRA guidelines to ensure they can absorb unexpected losses and to protect against insolvency. Broadly, insurers will design the reinsurance program they want for their specific portfolios, risk appetite and financial responsibilities, typically with the assistance of a reinsurance broker. Reinsurers will consider the insurer's preferences and conduct their own assessment in order to price for the risk they are taking on. This may involve looking at the historical performance of the portfolio to be reinsured or using risk models to determine a reinsurance premium.

Broadly, reinsurance arrangements can be categorised along the lines of being made on a 'proportional' or 'non-proportional' basis, and on a 'treaty' or 'facultative' basis. There are many different types of reinsurance that fall within these categories, but for the majority of Australian insurers writing policies that fall within the scope of the pool, the most prevalent types of reinsurance are treaty arrangements involving quota share (a type of proportional insurance) and excess of loss (a type of non-proportional insurance).[164]

160 McKinsey & Company, *SME insurance in Australia – A market ripe for change*, September 2017, p 18, accessed 5 September 2023.

161 QBE, *SME and Insurance: A pulse check on risk trends for businesses*, QBE website, 15 November 2019, accessed 5 September 2023.

162 ACCC, *NAII final report*, p 100.

163 ACCC, *NAII final report*, pp 61 and 82. ACCC, *First insurance monitoring report*, pp 44–45.

164 ACCC, *NAII final report*, p 13.

There are various types of reinsurance available to general insurers. However, most reinsurance can be commonly categorised as proportional and non-proportional reinsurance. Under proportional reinsurance arrangements, the reinsurer accepts a fixed percentage of both premiums and claims. Several insurers have purchased proportional reinsurance to reduce their total exposure and the amount of catastrophe reinsurance required.[165] Under non-proportional reinsurance, the insurer retains the cost of claims up to a certain threshold (the retention limit or excess) and the reinsurer pays the cost of claims above that point.[166]

In calculating the technical premium, the majority of insurers take into account the net costs of reinsurance. Net costs are the reinsurance premium less expected reinsurance recoveries (or payments from the reinsurer). The key issue for determining the reinsurance component of a technical premium for a policy is how the net reinsurance costs should be allocated to a policy level.[167]

Insurers do not necessarily take the same approach to allocating reinsurance costs. Many insurers allocate reinsurance costs to policies based on the amount that the risks covered by those policies will contribute to reinsurance costs.[168] On average, for any policy more likely to claim for high value amounts (for example, a property in a region at high cyclone risk), a larger reinsurance cost component will be applied compared to a property with a lower risk. The ARPC's reinsurance premiums for the pool are calculated at a property level but with an element of cross-subsidisation between low and high-risk properties, in order to direct savings to higher risk properties. How insurers plan to allocate these costs to retail premiums is discussed in Chapter 5.

4.2.3 Expenses and margin

A variety of expenses are incurred by insurers in supplying policies. They will also add a margin onto the costs once calculated.

Operating costs

Operating costs include things such as administrative expenses, marketing, and claims handling costs. These costs are relatively straightforward to predict for an insurer, and the key issue is how insurers allocate these costs across policies. Some insurers allocate most operating costs uniformly across Australia, but other insurers take the characteristics of the policy into account when allocating certain operating costs.[169]

Commission costs

Commission costs for an insurance policy will depend on the way the policy was purchased. Where a policy is purchased directly from an insurer, there will be no commission costs (although the operating costs component may be higher as the insurer will spend more on things such as marketing and sales when selling directly). However, where insurance is purchased through an insurer intermediary, as opposed to the insurer directly, there will usually be some commission included in the premium paid.[170] Commissions are usually calculated as a percentage of premiums, and therefore commission costs are generally higher in dollar terms in regions where premiums are also higher.[171]

165 ACCC, *NAII final report*, p 100.
166 ACCC, *NAII final report*, p 100.
167 ACCC, *NAII final report*, p 70.
168 ACCC, *NAII final report*, p 70.
169 ACCC, *NAII final report*, p 70.
170 ACCC, *NAII final report*, p 70.
171 ACCC, *NAII final report*, pp 71 and 102.

Margin

Once an insurer has determined the scale of the technical premium based on the costs of supplying the product, they will add a margin for profit and/or return on capital.[172] Insurers have outlined a wide variety of approaches to setting or achieving a margin. Margins often attempt to achieve overall profitability targets combined with required return of capital.

4.3 Premium adjustments and discounts

Once insurers determine the technical price, they will often make further premium adjustments to derive the retail premium. Decisions relating to premium adjustments are typically made by insurers with consideration to the impact across the whole portfolio and are not often visible to the consumer. Premium adjustments are often made in response to factors such as the insurer's aggregate concentration of risks and market position. These adjustments are generally made for commercial reasons and are less directly related to the individual risk of the property.[173]

By contrast, insurers may also offer explicit discounts for consumers for a variety of reasons, such as online purchase, no claims bonus or multi-policy discounts. Discounts are typically made on a policy level and may be applied to a premium after a retail premium is derived.[174]

The types of premium adjustment we consider in this section are:

- concentration risk
- market adjustments
- price optimisation
- premium capping and cupping.

We also consider some of the common discounts insurers provide to consumers.

This discussion is not intended to be an exhaustive list of the types of adjustments and discounts that insurers may make to their premiums. We note that the distinctions between adjustments and discounts are not always clear and that any adjustments may be driven by more than one of these considerations.[175]

4.3.1 Concentration risk

Concentration risk occurs when an insurer considers it has too much risk in an area, such that if there were a catastrophic event, the total loss to the insurer would be unacceptable. Exposure is a measure of the amount of risk that an insurer has in an area, or to a certain type of risk.[176] Premium adjustments to manage concentration risk or exposure occur where insurers increase their premiums above the technical premium to attempt to decrease the amount of risk they have in a particular area, or of a particular type.[177] For example, an insurer may monitor its share of high peril risk customers in a particular region, and where it reaches a level above its risk appetite it may implement measures such as embargoes or price increases to return the portfolio to an acceptable risk level.[178] We discuss these and other underwriting restrictions that insurers can use to limit their exposure in high-risk

172 ACCC, *NAII final report*, p 71.
173 ACCC, *NAII final report*, p 156.
174 ACCC, *NAII final report*, p 84.
175 ACCC, *NAII final report*, p 237.
176 ACCC, *NAII final report*, p 239.
177 ACCC, *NAII final report*, p 239.
178 ACCC, *NAII final report*, p 239.

areas or for perils outside of their risk appetite, and how the pool is designed to assist with availability by taking on insurers' cyclone risk, in Chapter 6.

4.3.2 Market adjustments

Consistent with the Northern Australia Insurance Inquiry, we found that insurers closely monitored competitors' pricing and adjusted their own pricing to maintain or achieve their desired market position.[179] Insurers' ability to set premiums that accurately reflect the risk of providing insurance is important to their ability to compete in a market. First, it helps an insurer set prices in a way that will ensure that it remains profitable. Secondly, it is important for sending the right price signals to consumers and helps the insurer to maintain the 'right mix' of risks.[180] By accurately setting the technical premiums, insurers are able to make the necessary adjustments to ensure pricing remains competitive. If an insurer sets premiums too high relative to the risk being insured, it is likely to lose business to more accurately priced competitors. Conversely, if an insurer sets its premiums too low, it may face 'anti-selection' where its share of high-risk customers increases, which can lead to high claims and reinsurance costs.[181]

4.3.3 Price optimisation

Insurers adjust premiums broadly to find a balance between the volume and profitability of policies written. These adjustments are made with reference to particular (usually non-risk related) characteristics of a customer such as their propensity to shop around, and to set premiums which they consider will maximise profitability and or customer retention.[182] What an insurer determines is 'optimal' will depend on the insurer's specific objectives and constraints. For example, some insurers may consider how profitable individual policies are alongside the insurers' competitive position in that region to determine an optimal premium change.[183] They may also consider how price sensitive customers are, choosing to price lower for more price sensitive customers, or price higher if customer retention is not negatively impacted.

4.3.4 Premium capping and cupping

Another premium adjustment tool used commonly in insurance is capping and cupping. Capping is used to moderate the amount that a retail premium can increase in a single year for a renewing customer. In this way it operates like a downward premium adjustment as it lowers the retail premium a customer would otherwise pay for insurance.[184] 'Cupping' or 'collaring' is a limit on the amount that a retail premium can decline in a year, for example, as a result of the insurer introducing new risk modelling. In this way it operates as an upward premium adjustment, because it increases the retail premium a customer would otherwise pay for insurance. We discuss how the pool may interact with insurers' capping and cupping adjustments in Section 5.4.

179 ACCC, *NAII final report*, p 237.
180 ACCC, *NAII final report*, p 124.
181 ACCC, *NAII final report*, p 124.
182 ACCC, *NAII final report*, p 233.
183 ACCC, *NAII final report*, p 244.
184 ACCC, *NAII final report*, p 241.

4.3.5 Discounts

In addition to the premium adjustments discussed above, there are a range of final discounts that insurers can apply to determine the final retail premium. Discounts are typically made at the policy level and can be given for the following:

- being a new customer
- being a longstanding customer[185]
- being a staff member of certain companies
- not making a claim over a specified period ('no claims bonus')
- bundling insurance products from the same insurer
- purchasing the product online.

Insurers typically offer the same types of discounts as each other, but the size of the discount may vary.[186] Discounts are often conditional on one or more criteria being met and may not be available to all customers in all areas.[187]

4.4 Surcharges, taxes and duties

Once the technical premium is determined and premium adjustments are applied, insurers then apply any surcharges they have determined, as well as taxes, duties or levies imposed by governments. This section provides an overview of these additional changes insurers apply to their premiums.

4.4.1 Surcharges

Insurers can also apply surcharges on premiums. Some, but not all insurers, will include a premium surcharge for consumers who pay by the month.[188] The ACCC found in the NAII final report that instalment surcharges are not so much a payment administration fee, but rather are reflective of what an insurer has assessed as a risk factor. That is, insurers consider that consumers who pay monthly are associated with higher claims costs than those customers who pay annually.[189]

185 While discounts by insurers for being a longstanding customer ('loyalty discounts') can have a direct impact on premiums, the NAII final report found that they may also serve to discourage consumers from switching brands. Further, ASIC has expressed concerns that any loyalty benefit for customers is reduced by the application of a 'loyalty tax', where an insurer considers a renewing customer's price elasticity and charges renewing customers who are less likely to shop around a higher premium than other customers. ACCC, *NAII final report*, p 125; ASIC, *Report* 765, p 21.

186 ACCC, *NAII final report*, p 85.

187 ACCC, *NAII final report*, p 85.

188 ACCC, *NAII final report*, p 86.

189 ACCC, *NAII final report*, p 361.

4.4.2 Taxes and duties

Taxes and duties applying to insurance include the GST and state and territory stamp duties and (in some jurisdictions) other levies. These are not a cost to the insurer, but they are an added cost incurred by the customer. Both are proportional to the premium, so the amount paid is higher in areas where premiums are higher.[190]

Some jurisdictions currently, or have previously, imposed levies on insurers to contribute to the funding of emergency services. Insurers then recover the cost of the levies from their customers, typically with reference to the premium paid. Levies of this kind are currently imposed on some insurance products in New South Wales and Tasmania.[191]

As stamp duties are applied on the GST-inclusive amount of a premium, the effect of these duties is magnified. For example, the combined GST and stamp duty taxes imposed on home insurance mean that premiums charged by insurers are magnified by between 19.9% to 22.1% depending on the jurisdiction (see Section 7.2 for more information).[192]

As premiums grow in northern Australia, so too does the dollar value of the amount paid in GST and stamp duty, as taxes are proportional to premiums.

190 ACCC, *NAII final report*, pp 54–55.

191 In September 2023, the Tasmanian Government released a draft Bill that proposed abolishing the business services levy: Felix Ellis, Minister for Police, Fire and Emergency Management, *Securing the future of our Fire and Emergency Services*, [media release], 28 September 2023. In November 2023, the NSW government proposed removing the emergency services levy from insurance bills in future: InsuranceNews.com.au, *NSW to ditch current insurance-funded Emergency Services Levy*, 16 November 2023, InsuranceNews website, accessed 17 November 2023.

192 Insurance duty was abolished in the ACT in 2016.

5. The expected impact of the pool on premiums

In this chapter, we discuss the expected or potential impact of the pool on the retail premiums paid by policyholders, noting that not all insurers have joined the pool at this time, and that many of those who have joined are implementing price changes over time. Our discussion reflects this transitional status of the pool at this time. Many of the challenges faced by insurers outlined in this chapter will resolve over time as the pool matures and as experience develops.

As outlined in Chapter 3, while the pool has been operational since July 2022, entry by insurers to date has been staggered, with different insurers at different stages of transitioning eligible policies into the pool and implementing associated changes to their pricing and other systems. Information provided by insurers indicates that this staggered approach to entry and systems changes is related to:

- required changes to peril modelling
- the need for insurers to quantify the 'gap' in coverage for cyclone losses incurred outside of the 48-hour claims period
- systems work needed to implement the pool into current pricing practices
- the desire of insurers to line up entry to the pool with the renewal of existing reinsurance arrangements.

These factors have affected the timing of insurer entry into the pool, but can also affect the way an insurer builds a retail premium and how it accounts for the changes in its reinsurance costs. These in turn can change the premium a policyholder will pay and the timing of that change.

This means that the actual impact of the pool is still to be determined. Accordingly, our discussion in this chapter takes a forward-looking approach to looking at the impact of the pool on premiums.

As set out in Section 5.1, an important part of examining the expected impact of the pool is how the ARPC has developed the reinsurance premiums charged to insurers, and how those premiums seek to direct savings to areas of medium to high risk of cyclone.

In Section 5.2, we outline the changes that the pool may require in insurers' peril modelling, particularly with respect to calculating cyclone-related damages sustained after the 48-hour claims period. We also discuss the administrative challenges insurers have stated they face in trying to incorporate the ARPC rating factors into their systems.

While eligible cyclone losses are covered by the pool, insurers may still need to purchase reinsurance from private markets to cover cyclone risk not covered by the pool and non-cyclonic risks such as flood or bushfire. The impact of the pool on reinsurance arrangements, including the perspectives of reinsurers, is discussed in Section 5.3.

Based on information we have obtained, insurers' modelled impacts of the pool on their business suggest the pool can deliver premium savings to some policyholders in northern Australia (see Section 5.4). However, the impact of the pool, particularly for those at medium to high risk of cyclone, will be heavily dependent on insurers' decisions relating to how any savings generated by the pool will be passed through to those intended to benefit.

In Section 5.5, we discuss the variety of different approaches to pass-through insurers have indicated they are taking (or intend to take) when implementing the pool, given the scope that is provided to them under the legislation relevant to the pool. Some insurers plan to ensure the exact reinsurance

premium charged by the ARPC will be allocated against a particular policy. Others plan to implement a staged approach to pass-through by initially passing on savings at an aggregated level, before transitioning to a one-to-one pass-through. Further, some insurers do not plan to implement a one-to-one pass-through, predominantly due to a preference to minimise system changes. All these different approaches create variability in the visibility of pass-through, and the expected impact of the pool on premiums, and may potentially limit savings for those policyholders who have undertaken private mitigation works (see Section 5.6).

Finally, we discuss when policyholders are likely to see any impact of the pool on their premiums in (see Section 5.7). The speed and process by which insurers choose to make changes to their pricing engines and the nature of the policy renewal cycle means it might be quite some time before some policyholders see benefits from the pool from their insurers.

5.1 ARPC reinsurance premiums and the expected savings from the pool

5.1.1 How the ARPC administers and operates the pool

As discussed in Chapter 1, the pool is intended to operate by the ARPC reinsuring a component of risk from insurers (cyclone and related flood risk) and charging insurers a reinsurance premium rate (to cover expected claims and operating expenses) without a margin.[193]

The ARPC's pricing formula sets the reinsurance premium rates that insurers must pay once participating in the pool. Collectively, the reinsurance premium rates seek to achieve an overall 'target premium pool' to meet the ARPC's expected cost of claims and operating expenses.[194] The actual reinsurance premium charged to an insurer for an eligible policy is based on the particular property's geographic location, building characteristics, and whether any mitigation activities have been undertaken to lower the risk of cyclone damage.

The principles which underpin the ARPC's pricing formula are for the pool to:

- be cost-neutral to government over the longer term
- lower the reinsurance cost for most policies with medium to high exposure to cyclone risk
- maintain incentives for risk reduction and offer discounts for properties that undertake mitigation
- encourage policyholders to engage in strategies to mitigate cyclone and related flooding risks.[195]

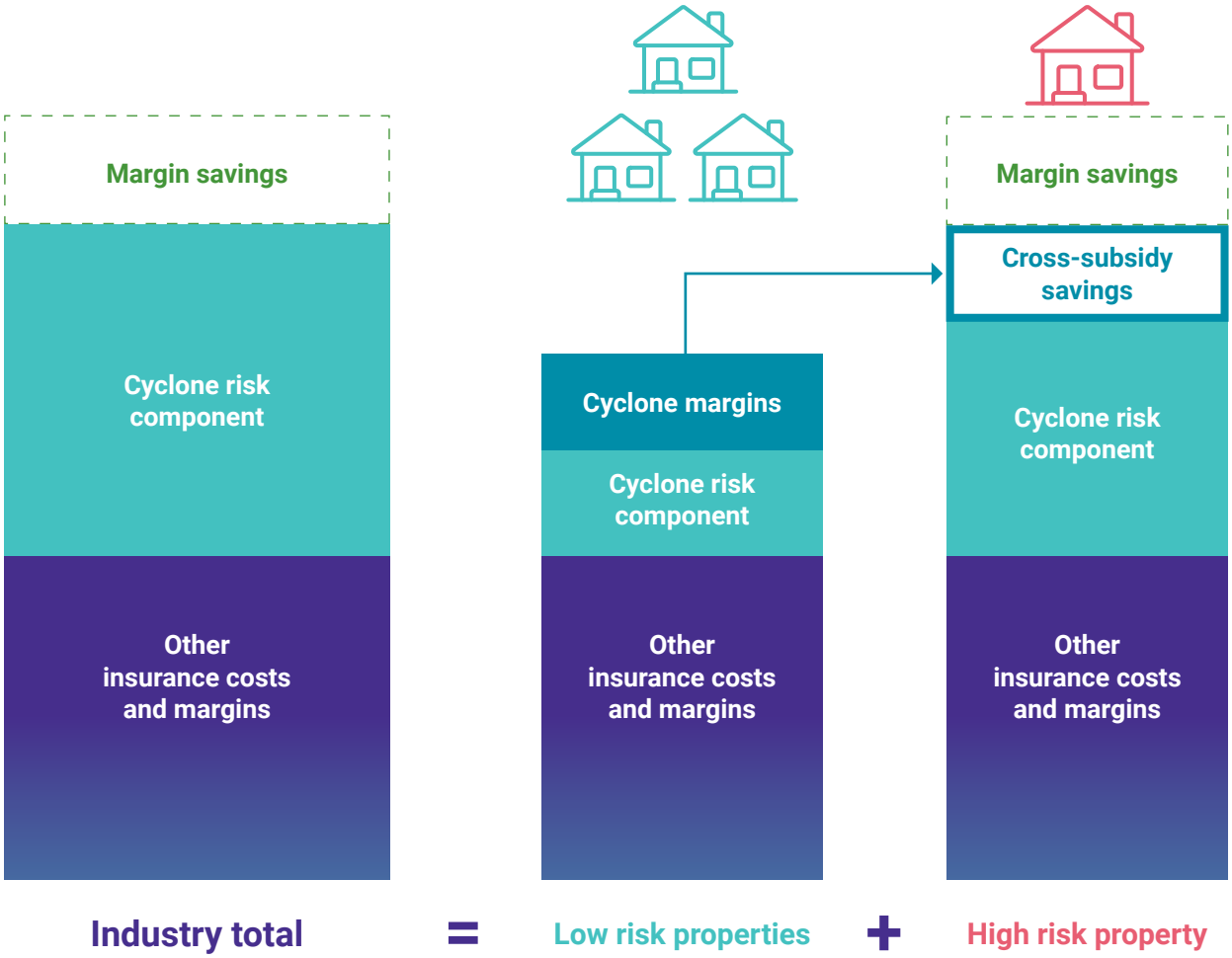
The government's intention is that, by forgoing a margin on the reinsurance the ARPC provides and requiring insurers to join the pool, the pool can set cross-subsidised reinsurance premium rates which lower the cost for properties at medium to high risk of cyclone, while keeping reinsurance premiums broadly comparable for properties at low-risk. This is illustrated in Figure 5.1.

193 ARPC, *ARPC – Premium Rate Assessment Report Update for Consultation – 1 October 2022(.PDF)* (October 2022 Premium Rate Assessment Report), ARPC website, September 2022, p 8.

194 ARPC, *October 2022 Premium Rate Assessment Report*, p 20.

195 ARPC, *Fact Sheet – Cyclone Reinsurance Pool*, ARPC website, accessed 6 September 2023.

Figure 5.1: Intent of pool premiums in delivering savings to medium and high cyclone risk policyholders



Source: Adapted from ARPC, *October 2022 Premium Rate Assessment Report*, p 7.

To set a reinsurance premium, the ARPC allocates each property a 'base rate' depending on the risk of cyclone in that location.[196] A series of risk rating factors (also known as 'modifiers' or 'risk relativities') are then applied to the base rate.[197] These rating factors reflect differences in relative risks, such as building characteristics that affect a property's resilience to cyclone events. For example:

- a house built after 1980 (or retrofitted) to meet building codes designed to withstand cyclonic winds is less likely to be damaged by a cyclone
- a house built on stilts is less likely to be damaged by flooding.[198]

The ARPC's rating factors include actions that property owners have taken to mitigate their cyclone risk. At present, the ARPC's pricing formula includes mitigation discounts for home insurance policies with roller door, window protection (cyclone shutters) or roof replacement mitigation actions.[199] If an

196 ARPC, *ARPC – CRP Premium Rate Assessment Report – reissued 8 July 2022 (.PDF)* (July 2022 Premium Rate Assessment Report), ARPC website, September 2022, p 23.

197 ARPC, *July 2022 Premium Rate Assessment Report*, p 25, Table 4.4.

198 ARPC, *July 2022 Premium Rate Assessment Report*, p 24.

199 ARPC, *July 2022 Premium Rate Assessment Report*, p 25.

insurer is unable to provide data on a particular rating factor, an 'unknown' option is applied.[200] The ARPC has stated that it will not unduly penalise insurers at the commencement of the pool for using unknown rates, except for year of construction, which it states all insurers should already collect.[201] However, the ARPC has signalled that the rates for 'unknowns' are likely to be revised upwards in time.[202]

As we have noted elsewhere in this report, there is no requirement under the legislation for insurers to directly pass on any savings from the pool to policyholders, or for a particular pass-through method to be used. The ARPC has outlined that the pool was deliberately designed to allow insurers a degree of discretion in passing on savings to policyholders.[203] This allows insurers the ability to smooth situations where increases may be large for particular policies or where insurer practices (such as commercial decisions to offer multipolicy or loyalty discounts) would have resulted in prices for some policyholders below what would be achieved using the ARPC's pricing formula.

The ARPC has stated that it expects the market to increasingly reflect the pool's reinsurance premiums at the policy level over time to best achieve the intent of the pool in directing support to properties at medium to high risk of cyclone. However, it has stated this will not be 'realistic' during insurers' transition to the pool.[204]

5.1.2 ARPC's estimates of retail premium outcomes for policyholders

Table 5.1 below summarises the ARPC's estimated total reductions in policyholder retail premiums when applying its October 2022 premium formula to model the reinsurance costs for insurers compared to existing reinsurance expense.

The table is based on the ARPC's analysis of a large sample of data[205] provided by certain insurers for residential home (720,924 policies), SME (34,700 policies) and strata (24,508 policies), and modelling of the impact on policyholder premiums of insurers joining the pool. The ARPC's estimates are presented by reference to:

- 'all record samples' that the ARPC analysed – across areas of Queensland, the Northern Territory, Western Australia and northern New South Wales that have some cyclone risk
- policies within the record sample that cover any part of northern Australia[206]
- policies in northern Australia that currently pay the highest premiums, being those home and SME policies paying over $1.50 per $100 sum insured.

Table 5.1 reflects the ARPC's expectation that, consistent with the government's intention, savings will be higher in northern Australia than they will be across the entire set of policies that have some cyclone risk, and also that northern Australian policyholders currently paying the highest premiums will get the greatest savings.[207]

200 ARPC, *July 2022 Premium Rate Assessment Report*, p 25.

201 ARPC, *July 2022 Premium Rate Assessment Report*, p 25.

202 ARPC, *July 2022 Premium Rate Assessment Report*, p 25.

203 ARPC, *July 2022 Premium Rate Assessment Report*, p 26.

204 ARPC, *October 2022 Premium Rate Assessment Report*, p 26.

205 The ARPC could not reliably estimate savings for high-risk strata policies due to data limitations. With respect to estimates for 'high total premium' policies, the ARPC noted that the total premium can be high for reasons not just related to cyclone risk, such as if a home has exposures to other natural perils or the SME business involves dealing with hazardous materials. (ARPC, *October 2022 Premium Rate Assessment Report*, p 25).

206 Insurers often evaluate natural hazard risk in particular geographic areas by reference to 'Catastrophe Risk Evaluation and Standardising Target Accumulations' (CRESTA) zones. The ARPC used CRESTA zones 5–20 as a proxy for northern Australia when estimating the potential impact of the Pool on policyholders' premiums.

207 ARPC, *October 2022 Premium Rate Assessment Report*, p 5.

Table 5.1: ARPC's summary of estimated average premium savings by class (1 October 2022 rates)

Product class	All record samples	Northern Australia	High total premium band in Northern Australia	Total sample size
Home	-6% (720,934)	-13% (143,500)	-32% (2,416)	720,934
SME (policies with building cover)	-6% (34,700)	-10% (11,857)	-13% (274)	34,700
Strata	-14% (24,508)	-37% (1,905)	N/A	24,508

Source: ARPC, *October 2022 Premium Rate Assessment Report*, p 25.

The ARPC noted that caution is needed in interpreting the estimated savings for several reasons.[208] First, these projections assumed that a one-to-one pass-through of savings to policyholders will occur. That is, the ARPC's estimated savings presume that insurers will directly reflect the ARPC's premiums in insurers' own pricing to policyholders.[209] However, the design of the pool means that 'actual policyholder outcomes will result from the totality of pricing decisions made by insurers'.[210] The pass-through of reinsurance premiums to policyholders is discussed in detail in Section 5.5 and will be a key focus of our monitoring role.

The ARPC modelling also assumes that all other economic factors affecting insurance prices are held equal. The ARPC notes that in practice, however, economic factors such as the hardening reinsurance market, high inflation and global supply chain issues placing upward pressure on insurance premiums may make it difficult to observe any premium reductions arising from the pool.[211] As set out in Chapter 2, there are many factors which can affect insurance prices.

Finally, the estimates outlined in Table 5.1 are an average of the estimated impact of the pool on policyholder premiums. The actual outcomes will vary for particular policyholders and insurers. As illustrated in Table 5.2, some home insurance policies may attract a higher reinsurance premium than they would have otherwise had allocated against their policy for eligible cyclone losses.[212] Actual reinsurance costs for home, strata and small business policies are provided in Chapters 7, 8 and 9 and will be monitored over the course of our role as insurers continue to implement the pool.

208 ARPC, *October 2022 Premium Rate Assessment Report*, p 11.

209 ARPC, *October 2022 Premium Rate Assessment Report*, p 11.

210 ARPC, *October 2022 Premium Rate Assessment Report*, p 11.

211 ARPC, *October 2022 Premium Rate Assessment Report*, p 5.

212 The ARPC used CRESTA zones 1–22 and 49 as a proxy for 'all cyclone affected areas' in Australia. This includes, for example, southern Queensland and other parts of Australia that are not located in northern Australia but are exposed to some (including low) cyclone risk.

Table 5.2: ARPC's estimated premium impact distribution for home insurance policies by region

Premium impact of the pool	Northern Queensland	Rest of Queensland	Northern Australia	All cyclone affected areas
Increase >20%	1%	2%	1%	2%
Increase 10–20%	2%	2%	2%	2%
Increase 5–10%	3%	4%	3%	5%
Increase 0–5%	9%	14%	9%	20%
Decrease 0–5%	35%	38%	35%	35%
Decrease 5–10%	13%	20%	13%	16%
Decrease 10–20%	17%	15%	17%	12%
Decrease >20%	20%	5%	20%	7%

Source: ARPC, *October 2022 Premium Rate Assessment Report*, p 27.

Note: For this analysis, ARPC defined Northern Queensland as CRESTA zones 5–15, Rest of Queensland was defined as CRESTA zones 1–4, Northern Australia was defined as CRESTA zones 5–20 and all cyclone affected areas were defined as CRESTA zones 1–22 and 49.

5.2 The impact of the pool on insurers' internal pricing processes

The implementation of a policy intervention like the pool will necessitate changes by insurers to their business operations. In this section, we discuss changes insurers need to make to their peril modelling as a result of the pool, particularly with respect to calculating cyclone-related damages sustained after the 48-hour claims period. We also discuss the administrative issues insurers have raised when trying to incorporate the ARPC rating factors into their existing systems.

5.2.1 Implementation of the pool requires changes to peril modelling

Information provided by insurers indicates that implementing the pool is not as straightforward as replacing the expected claims costs for cyclone with the ARPC premium. As outlined in Chapter 4, natural peril claims modelling is complex and typically requires a significant amount of data. With respect to cyclone risk, insurers are likely to use a combination of internal and external models to determine the cyclone component of the premium for a particular policy. Each of these models could use different definitions, assumptions, and inclusions resulting in different estimates. These differences in approaches means that identifying perils covered by the pool needs careful consideration by insurers to ensure a close approximation of the risk. For example, one insurer has not previously rated premiums for cyclone as a separate peril and has instead historically modelled expected cyclone costs under the broader banner of 'storm'. Another has had to adjust flood modelling to avoid double counting of flood damage caused by cyclone.

Insurers have considered that isolating cyclone risk from current pricing approaches is further complicated by the 'cyclone event period' defined by the legislation. The 'cyclone event period' covers losses arising during a 'cyclone event' which lasts from the time a cyclone begins until 48-hours after the cyclone ends. Any damages arising outside of this window will not be covered by the pool.

While the ARPC published modelling to assist insurers with the determination of flood losses likely to be covered by the pool, the division between cyclone damage before and after a 48-hour period

following the downgrade of a cyclone was not previously part of insurers' modelling. As a result, it continues to be raised as a concern by insurers about how they implement the pool.[213] Of note, one insurer expects claims modelling issues relating to rain, rainwater runoff and riverine flooding associated with cyclone outside the 48-hour period, and considers that it will be difficult to calculate these losses, as they are not directly available in existing industry models. Similarly, another insurer stated that new flood models were needed to calculate exposure for risks (particularly flooding) outside the pool.

Documents obtained from insurers show a wide range of estimates for the percentage of cyclone-related flooding that is covered by the pool. This is predominantly due to differences in insurers' exposure, as flood related losses will be more likely to be covered by the pool in northern coastal regions which are more at risk of cyclone (and by extension, the risk of cyclone-related flooding that occurs within the 48-hour claims period). An insurer with a large presence in northern Australia stated it anticipated ceding approximately 50% of cyclone-related flooding risk. Another insurer that limits its exposure to risks in northern Australia estimated that approximately 12% of its current flood risk is cyclone related.

Insurers indicated the 48-hour claims period in the pool's design means they still need to seek reinsurance from the private market to remain protected from those cyclone-related losses, particularly from riverine flooding, occurring more than 48-hours after the declared end of a cyclone.[214] For example, one insurer highlighted uncertainty relating to the impacts of the pool on product coverage and other risks and the need to continue getting a better understanding of the impacts of joining the pool.

5.2.2 Incorporation of ARPC rating factors into insurer systems

Insurers highlighted concerns around the business complexity of amending their internal systems to ensure compatibility with the ARPC's rating factors.[215] Compatibility with the ARPC rating factors is important, as this will ultimately influence the extent of savings the pool will be able to generate for insurers and, ultimately, policyholders. For example, an insurer that has the existing ability to collect all of the rating factors or has determined to make changes to its systems to enable it to do so, will be able to benefit from reduced rates offered by the ARPC for properties with characteristics which reduce its risk of cyclone damage. However, if an insurer does not capture a rating factor, the 'unknown' relativity will be applied, which is generally the highest factor and therefore more expensive.

This means that, although in theory the reinsurance premium for any one property will be the same for all insurers, differences in the data collected by insurers may lead to different outcomes and consequently a different quantum of savings that could be achieved and passed on to policyholders. For example, if Insurer A captures relevant risk details not captured by Insurer B, the reinsurance premium will vary (and likely be higher for Insurer B).

RACQ has stated that entry into the pool requires 'a lot of systems and data work' to get right.[216] Some insurers raised concerns that the pool formula is difficult to replicate in their internal systems. An insurer detailed how its cyclone sum insured pricing structure is different from the ARPC's premium formula, with different components and rating factors. In addition to system and technology limitations and cost implications, this creates a need to reallocate the net cost of reinsurance and return on capital that was applicable to cyclone (and related flood and storm surge perils) to non-cyclone perils. Further, even when some rating factors are collected by insurers, this can still

213 ARPC, *Cyclone Reinsurance Pool – Determination of Cyclone Related Flood Proportions [PDF 2.8MB]*, accessed 5 October 2023.

214 ACCC, *First insurance monitoring report*, p 51.

215 ACCC, *First insurance monitoring report*, p 48.

216 Mr Trent Sayers, Group Executive Insurance, RACQ, *Proof Committee Hansard, 25 November 2022 [PDF 804KB]*, p 14, accessed 11 August 2023.

result in variances. One insurer noted that differences between the ARPC's pricing and its own pricing differs widely at the policy level. This is because the ARPC uses different rating factors, and even rating factors which they do have in common hold a different view of the risk.

Variances between insurer pricing approaches and the ARPC's premium calculation methodology was an inevitable by-product of the pool's design. The standardisation embedded in the ARPC pricing formula ensures that all insurers receive the same price for reinsurance and support can be effectively targeted to properties at medium to high risk of cyclone (as intended by the design of the pool). While the challenges for insurers of incorporating the ARPC rating factors are live concerns now in this transitional period, the required changes to insurers' systems arising from the pool may lead to better data capture across the industry in the longer term.

5.3 Impact of the pool on pre-existing reinsurance arrangements

The pool has been designed to improve affordability and availability of insurance in cyclone prone areas through reducing the cost and improving the affordability of reinsurance to insurers. However, it does this in the context of pre-existing reinsurance arrangements which now must be reconsidered by insurers. In this section, we outline insurers' views on the impact of these changes and we also provide an overview of reinsurers' perspectives.

5.3.1 Removing or reducing cyclone cover from current reinsurance arrangements

Many insurers indicated that there were complexities in amending their current reinsurance arrangements in order to join the pool. Accordingly, insurers are carefully considering their approach to other private reinsurance when planning their entry to the pool. For example, one insurer described the manner and extent to which risks are covered by the pool as having a 'major knock-on effect' to its probable maximum loss and overall reinsurance cover it requires. That insurer is considering the potential for the pool to increase the complexity of its reinsurance program in 2024 due to changes in its reinsurance needs and risk profile.

Implementing the pool necessitates changes to insurers' typical reinsurance arrangements as many reinsurance contracts are typically taken out on a 'whole of portfolio' basis across a number of different natural perils.[217] Documents from one insurer indicated that the market generally does not distinguish cyclone as a distinct peril in existing reinsurance arrangements. As discussed in Section 5.2, insurer documents have detailed difficulties with splitting out their perils when considering entry into the pool. For example, one insurer explained it will need to separate cyclone-related flood and non-cyclone-related flood out of total flood, and considered that this has implications for reinsurance and the cost of capital expenses.

Another insurer is considering splitting its 'storm' peril into several new perils, which includes cyclone risk retained by the insurer and cyclone risk ceded to the ARPC. This insurer is considering the historical and reporting implications of doing so, in addition to the additional IT system work that is required.

Another insurer considered that, as a result of the pool removing cyclone related risks, there will likely be additional reinsurance costs allocated to other natural hazard perils.

217 ACCC, *First insurance monitoring report*, p 53.

As with other issues about pool implementation, insurers are resolving or reaching conclusions on some of these issues as time passes and they join or get closer to joining the pool. However, in some cases, the issues remain live considerations for insurers that will be adjusted over time.

5.3.2 Factors outside the pool are increasing the price of reinsurance

The specific effect of the pool on insurers' private reinsurance arrangements is obscured and complicated by the timing of entry varying between insurers, differences in what insurers choose to cede to the pool and how, and increased reinsurance prices overall. Further, current market conditions indicate that reinsurance factors unrelated to cyclone risk have been affecting the private reinsurance market and could impact whether policyholders see the extent of benefits estimated by the ARPC.

As discussed in Chapter 2, the hardening reinsurance market and recent severe weather events have resulted in many insurers reporting increased reinsurance prices.[218] This hardening market has influenced the way insurers have approached their overall reinsurance strategies in 2023, including the types of private reinsurance arrangements they have, with some insurers choosing to retain more risk rather than to cede risk to reinsurers.

For example, following its 2023 reinsurance renewals, IAG stated that it increased its first event retention in order to minimise the impact of increasing reinsurance prices on customers.[219] This was due to inflation and global reinsurance market impacts.[220] Due to rising reinsurance prices, Suncorp also amended its 2024 reinsurance strategy by increasing retention for a first large event, and deciding not to renew its aggregate excess of loss reinsurance (a type of reinsurance that offers protection against an accumulation of losses, such as in relation to smaller weather events).[221] Reinsurance prices have been cited by some insurers as a driver behind the need to increase the price of retail insurance premiums.[222] Overall, the impact of the prices charged for reinsurance, due to both the pool and external factors, will become clearer as insurers join the pool throughout 2023–24 and these costs are reflected in insurance premiums.

5.3.3 Reinsurer views on the impact of the pool

As noted in Section 1.3, we issued a voluntary information request to reinsurers to obtain their views in relation to the pool and the reinsurance market more broadly. We have sought this information because the introduction of the pool changes the risks that insurers cede to reinsurers, and this results in changes to reinsurance arrangements. Additionally, in 2022, the ACCC found that the renewal and renegotiation of insurers' existing reinsurance contracts was a major factor affecting timing of pool entry by insurers and their views on the extent of potential costs and premium savings. Reinsurers' views and their experience with recent reinsurance renewals and negotiations after the commencement of the pool can provide context to these issues.

Overall, the responses received indicate that the removal of cyclone risk from private reinsurance arrangements due to the implementation of the pool was or will be reflected in reinsurance renewals, as insurers are purchasing less cyclone reinsurance from the private market. It was noted publicly that the pool eased demand for private reinsurance during 2023 mid-year renewals as it resulted

218 Suncorp, *Message form the Chairman FY 23*, accessed 30 August 2023; Swiss Re Group, *The State of the Reinsurance Property Catastrophe Market*, 16 May 2023, accessed 30 August 2023; QBE, *How Global Events Can Affect Reinsurance*, 5 July 2023, accessed 30 August 2023.

219 IAG, *IAG confirms 2023 reinsurance program and 10% quota share renewals*, 10 January 2023, accessed 21 July 2023.

220 IAG, *IAG confirms 2023 reinsurance program and 10% quota share renewals*, 10 January 2023, accessed 21 July 2023.

221 Suncorp, *FY24 Reinsurance Program update [PDF 231KB]*, 4 July 2023 accessed 12 July 2023, p 1.

222 Suncorp, *FY24 Reinsurance Program update [PDF 231KB]*, 4 July 2023 accessed 12 July 2023, p 2.

in increased overall capacity in reinsurance markets.[223] The documents we obtained indicated that there is still a residual amount of cyclone peril coverage being purchased from the private reinsurance market. One reinsurer has indicated that this residual risk (that is, non-eligible risks and home, strata and small business policies suffering losses incurred more than 48-hours after the cyclone ends) may be in the order of 20%.

Reinsurers have also noted elements of the pool's design may potentially impact insurers' reinsurance programs. These elements relate to issues raised by insurers discussed in Section 5.2, including remaining uncertainty around the 48-hour period of coverage provided by the pool, and the residual risk that will need to be captured in reinsurance contracts outside of the pool. The adequacy of coverage has not yet been tested, with one reinsurer noting there 'continues to be areas of uncertainty in how the actual mechanics of the pool will operate until fully tested by a relevant cyclone event.' In relation to potential gaps in coverage and modelling issues, one reinsurer also discussed that the final responsibility for ensuring that a reinsurance contract provides adequate cover rests with the insurer. However, that reinsurer also indicated that reinsurers do take an interest in whether the coverage offered to insurers is appropriate, given the long-term, strategic nature of relationships between insurers and reinsurers. If it were to identify any material gaps, it would outline these to the insurer for the insurer to make an informed decision.

As noted in the ACCC's first monitoring report, some insurers made claims that removing (or substantially reducing) private reinsurers' ability to cover cyclone-related events would effectively increase reinsurers' relative exposure to other non-cyclone-related risks in Australia, and that this reduction in risk diversification may result in reinsurers increasing premiums for non-cyclone risks.[224] In practice, this year reinsurer views in relation to the pool's effect on risk diversification have been mixed. Several reinsurers indicated there has been a reduction in risk diversification as a result of the pool, but some reinsurers consider this change in risk diversification has had minimal impact on price in reinsurance negotiations for the 2023 cycle. One reinsurer indicated that the impact on risk diversification was modest from a global portfolio perspective, but significantly greater for business written within its Australian branch. Another reinsurer discussed how the Australian and New Zealand catastrophe market is part of a multi-peril, multi-geographical program, and that removing a part of cyclone risk in one country does not have a significant impact from a diversification point of view. Another reinsurer noted that the impact to diversification from the removal of eligible cyclone risk from reinsurance programs can be more pronounced, especially where cyclone risk from eligible policies constitutes a large component of the insurer's overall risk profile. Further information about broad, global market impacts on risk diversification is discussed in Chapter 2.

In addition to the pool impacting reinsurance negotiations and arrangements, reinsurance renewals are also occurring in the context of a hardening reinsurance market, as discussed above. Additional factors influencing reinsurance prices that were discussed by one reinsurer include an increase in secondary peril events, and inflation. For example, this reinsurer also noted that 'whilst the removal of cyclone exposure leads to a reduction of modelled exposure, the overall impact might still be a year-on-year dollar price increase as the benefit from the cyclone pool was more than offset by a risk reset of other perils, including adjustments for inflation'. We note that these other perils may have a different geographic and risk profile to the cyclone risks being addressed by the pool.

223 Aon, *Reinsurance Market Dynamics [PDF 749KB]*, June and July 2023, accessed 7 September 2023.

224 Australian Parliament, *Senate Economics Legislation Committee Hansard; Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Bill 2022*, 8 March 2022, p 17, accessed 30 November 2022; Suncorp, *Submission to the ACCC Northern Australia Insurance Inquiry Second Update Report*, 3 September 2019, p 5; Insurance Council of Australia, *Insurance Council of Australia submission to Cyclone Reinsurance Pool Taskforce, exposure draft legislation consultation [PDF 191KB]*, 17 December 2021, p 3.

5.4 Insurers' modelling of potential savings for policyholders

Insurers have reported a wide range of potential outcomes for policyholders arising from the pool. The results are dependent on a variety of factors including the geographical location of the property, its characteristics, and the type of insurance cover purchased.[225]

Some insurers noted that they anticipate an average decrease for northern Australia home and contents premiums by more than the 13% decrease estimated by the ARPC in October 2022. One insurer states that, even after allowing for year-on-year changes, entering the pool offers significant premium decreases on average for customers in northern Australia of approximately 19%. Another insurer anticipated that some customers with policies under its home and contents portfolio in high cyclone risk areas will 'see a price decrease of more than 20% relative to current rates.'

As intended by the design of the pool, the benefits are more subdued when accounting for policyholders that reside in low cyclone risk areas. Two insurers indicated their customers are likely to see an average decrease of 6%. Another insurer stated that it does not anticipate any savings from the pool within its first year of entry due to the higher cost of the ARPC reinsurance coverage compared to its previous program.

Some insurers continue to express concern that the pool will result in higher premiums for customers in low cyclone-risk areas due to the cross-subsidisation inherent in the ARPC rates. One insurer noted that it anticipates price increases for some customers in low cyclone-risk areas in the order of 6%–10% 'due to the pool directly funding some of the premium reduction in high-risk areas with premiums from low-risk areas'. An additional view raised by one insurer is that the pool will have an unfavourable impact on its aims to grow its business in southeast Queensland, due to the level of cross-subsidisation in the cyclone reinsurance premium. We note that, to an extent, these perspectives likely reflect the different approaches taken by some insurers to focus on offering business in lower cyclone risk regions rather than higher cyclone risk regions. Insurers offering wider geographic coverage with a range of customers in low to higher cyclone risk areas may be less concerned overall about cross-subsidisation, as some of their customers will benefit from this element of the pool's design.

Information we obtained suggests that savings for SME customers are heavily dependent on the type of cover provided. One insurer indicated that although it anticipates the pool will provide an overall saving for SME customers, business interruption cover will experience a premium increase of up to 10% to match the ARPC reinsurance costs for business interruption cover.

The information available from insurers on the impact of the pool on strata premiums was more limited. This may be due to several factors including the more limited number of insurers in our sample providing this type of insurance, strata properties being less uniform (which may complicate modelling) and the higher number of intermediaries involved (which may influence insurers' end to end visibility of the pool's effect on premium prices). Information from one insurer suggested that the potential strata savings were dependent on which of its brands was being considered. One brand's premium was expected to increase on average 4% due to the pool while another brand's premium under the same insurer was expected to decrease on average 6%. The insurer noted that these differing results were driven primarily by existing premium capping being lower than the proposed ARPC premium.

While these modelled outcomes reflect what insurers anticipate the impact of the pool will be overall, the actual result for individual policyholders will be heavily dependent on insurers' decisions relating

225 Estimates provided by insurers on the impact of the pool on premium estimates may or may not consider outside influences on premium prices, such as the offsetting effects of inflation or increases in non-cyclone reinsurance costs.

to how any savings generated by the pool will be passed through to those it is intended to benefit, which we discuss below in Section 5.5.

5.5 Insurers' approaches to pass-through

As outlined in Section 5.1.2, the ARPC's estimates of the pool's savings are modelled based on the assumption that all insurers are able to implement a 'one-to-one pass-through'. In effect, this would mean that the actual reinsurance premium charged for a particular property would be passed on to its respective policyholder.

However, it is not mandatory for insurers to implement a one-to-one pass-through. Insurers have the discretion to decide:

- how to incorporate the ARPC rates into their pricing systems (e.g., some may choose to store the reinsurance premiums 'off-system' or fully implement the ARPC rating factors into their pricing infrastructure[226])
- how to pass the reinsurance premiums through to their policyholders.

The ARPC considers that this flexibility should allow insurers to adjust to any unexpected consequences of incorporating the reinsurance premiums into their pricing systems, for example where some of the insurer's existing premium rates are below the rates indicated by the ARPC's pricing formula.[227]

At present, there are a wide range of proposed approaches across insurers. Four insurers have indicated plans to implement a one-to-one level pass-through. Of these 4 insurers, 2 are planning to implement a staged pass-through, whereby they intend to move to a one-to-one pass-through after a period of time in the pool using an alternative approach. An insurer planned to build the 3 ARPC premium components (wind, flood and surge) directly into its pricing engine to enable the benefits of the pool to be passed to their policyholders. The same insurer also planned to remove any discounts or premium adjustments (e.g. capping or cupping) from the cyclone and flood-related cyclone pool components. Another insurer is planning to update the new premium rating configuration for its home product by introducing new peril components (for the ARPC's premium rates for wind and flood), and reducing the retained claims cost and reinsurer cost components to account for the eligible risks ceded post-entry to the pool.

Comparatively, other insurers have indicated they will be using alternative approaches to a one-to-one pass-through of the ARPC premium rates. Some insurers plan to first calculate the overall pricing impacts of the ARPC reinsurance premiums at a high level before passing on pricing changes to individual policyholders.

One insurer describes its approach to pass-through as follows: 'The agreed approach is not to charge the ARPC rate at individual risk level, rather continue with the [insurer's] current rating methodology, continuing to align at [the] portfolio level to future ARPC rate changes'. Another insurer is planning to approach the pass-through by 'attempting to retrofit the ARPC outcomes into its customer pricing by adjusting algorithm parameters'.

Additionally, one insurer has used different approaches to pass-through depending on the region and product. This insurer noted that adjustments would be made at a CRESTA level for some landlord and farm products where it does not capture explicit cyclone ratings. For all other home and landlord products, the insurer planned to replace the existing cyclone peril with an approximation of the ARPC premium, as the ARPC rating structure is different to its existing cyclone wind peril structure, and it sought to retain its current discount structure.

226 ARPC, *October 2022 Premium Rate Assessment Report*, p 5.

227 ARPC, *October 2022 Premium Rate Assessment Report*, p 33.

We note that some insurers not looking to adopt a one-to-one pass-through approach have indicated they are primarily doing so due to systems/data limitations and/or existing pricing practices. One insurer estimated that replicating the ARPC rating factors into its pricing engine would cost it approximately $50 million. Some insurers implementing an alternative approach to pass-through also expressed a preference to maintain most of their existing systems, processes and pricing approaches. Another insurer noted that implementing an alternative approach to pass-through is beneficial because it allows existing important internal pricing metrics and rating methodology to be maintained over time.

Insurers' business objectives are another key consideration in their planned pass-through approaches. The funds required from low cyclone risk properties to subsidise medium to high cyclone risk properties, and any differences in the perceived cyclone risk of a particular property under the pool, will mean some policyholders will experience an increase in their premium. The ARPC modelling anticipates up to 29% of home policies across cyclone affected areas will experience an increase if one-to-one pass-through occurs. Most of these premium increases will be in the order of up to 5%, but some may experience increases over 20%.[228] We understand insurers are therefore considering the overall impact of the pool holistically on their business and any potential flow on effects in relation to customer retention, market positioning and competitiveness. For example, one insurer outlined its focus was on opportunities in low cyclone risk areas, noting it does not make commercial sense to reduce premiums of clients who are already happy with their premiums and increase others, potentially losing them and reputation in the process.

The extent to which insurers give weight to these competing objectives in determining their approach to pass-through may mean that the objectives of the pool in targeting support to those at medium to high risk of cyclone are dulled. Approaches which do not implement a one-to-one pass-through also make it more difficult to assess the extent of the pool's impact on premiums.

We note that some insurers, particularly those smaller insurers with a mandatory entry date of 31 December 2024, are yet to decide on a definitive approach to pass-through. Some insurers have indicated a preference for one-to-one level pass-through but at this stage, their implementation approach has not been finalised.

We have also had discussions with some insurers that indicate their approach is evolving as they implement the pool and get closer to entry or actually join the pool. It should be noted that while insurers are not looking to adopt a one-to-one pass-through immediately, they may do so at a later point in time. To achieve entry into the pool in a timely manner, some insurers have adopted a staged approach to pool implementation. Documents provided indicate that at least 2 insurers have entered the pool with a view to passing on the 'shape' of the ARPC premiums at an aggregated level on entry. Both insurers outlined plans for changes to their systems and processes to pass on the ARPC premiums at the one-to-one level over a longer period.

Insurers stated that there are several advantages of a staged approach. One insurer outlined that the staged approach enables it to meet the requirement to enter the pool by the required date while allowing it to prioritise deliverables that are considered mandatory, and progress other strategic work that could improve the efficiency of its business operations in the long term. Another insurer stated that the interim stage allows it to focus on 'back of house' changes, such as reporting, analytics and the pricing engine before shifting focus to introduce the full suite of rating factors used by the ARPC. Other advantages mentioned by insurers include the ability to:

- manage any risks associated with incorrect assumptions in modelling and or premium calculations, which may result in re-work and delays
- spread out the cost of implementing the project in tranches to minimise the risk of budget overspend

228 ARPC, *October 2022 Premium Rate Assessment Report*, p 30.

- manage reputational risks if they do not pass on the savings at the policy level, noting that this may potentially lead to competitive disadvantage and media scrutiny.

While a staged approach may make business sense for insurers, from a policyholders' perspective it means delays from the insurer's entry into the pool until the full benefit of the pool may be reflected in their premium, particularly for those in high cyclone risk regions. The various factors which impact the timing of benefits coming into effect for some policyholders, depending on their insurer, are discussed further in Section 5.7.

5.6 Incorporation of mitigation rating factors into insurer systems

In line with the legislative objectives of the pool, the ARPC's pricing formula includes incentives for risk reduction and offers discounts for properties that have undertaken mitigation.[229] At this stage, the ARPC has provided risk mitigation relativities for its home building premium rates. These cover the following areas of mitigation:[230]

- Roller door bracing – a discount applies if the roller door is compliant with AS4505-2012 on homes built pre-2012.
- Window protection – a discount applies for houses that have protection (i.e., cyclone shutters) on all windows.
- Roof mitigation – a discount applies for houses built pre-1982 where roof structures have been upgraded with tie-downs (i.e. over-batten roof systems) or a complete roof replacement and structure tie-down upgrades have been made to current standards.

The ARPC has stated that the discounts and risk mitigation work will assist in improving the affordability and sustainability of property insurance over time.[231] However, while insurers often assess the cyclone or flood risk at an address level, several insurers currently do not have measures in place which allow them to take household level mitigation activity into account. As a result, consumers who have undertaken works to improve the resilience of their property do not always see the benefit of this through lower insurance premiums.[232]

While insurers initially expressed support for incorporating risk mitigation into the pool's pricing formula[233], some have indicated in their documents that implementing the mitigation rating factors has not been straightforward. Information we have received from insurers indicates that there can be costs involved in capturing this information. One insurer indicated that it had not yet quantified the costs of implementing all of the mitigation factors as it was some time away from full implementation of the ARPC's rating factors.

Some insurers that already collect some of the information required by the ARPC for their mitigation discounts have raised concerns about the effectiveness of the ARPC's mitigation rating factors to provide the correct risk pricing signal. One insurer indicated that it does not believe the pool will encourage mitigation because it considers the ARPC's mitigation discounts to be too limited in scope and variety. Another insurer noted that only a small number of customers would 'materially benefit from discounts due to mitigation' given that it writes only a small proportion of its policies in high cyclone-risk areas. Additionally, one insurer raised that the removal of its current cyclone mitigation

229 ARPC, *Insurer Onboarding*, ARPC website, accessed 27 July 2023.

230 ARPC, *October 2022 Premium Rate Assessment Report*.

231 ARPC, *Insurer Onboarding*, ARPC website, accessed 27 July 2023.

232 ACCC, *NAII final report*, p 514; ASBFEO, *Small Business Natural Disaster Preparedness and Resilience Inquiry Report*, accessed 5 September 2023, p 38.

233 ACCC, *First insurance monitoring report*, p 56.

discount and a move to policy-level peril pricing means that some of their existing customers are at risk of a 'premium shock' due to price increases.

Insurer hesitancy to capture and include incentives for mitigation has the potential to undermine efforts to incentivise private mitigation works. In addition, those policyholders who have undertaken activities to reduce the risk to their property will not experience the benefit of the discount if the insurer does not capture those risk reduction activities. As per the ARPC formula, if an insurer does not capture a rating factor, the policyholder will get the default relativity, which is generally the highest factor and therefore the most expensive to the policy. However, insurers may improve their capability and systems to enable better capture of the rating factors over time.

5.7 When the pool is expected to impact retail premiums

As outlined in Chapter 3, most large insurers have joined the pool at the time of release of this report. However, based on information we have received from insurers, it may take some time before policyholders see any savings arising from the pool reflected in their retail premiums, depending on their insurer. In this section, we discuss the factors influencing the timing of the pool's impact on retail premiums. Chapter 3 provides an overview of insurers' considerations in determining their timing of entry into the pool.

The most obvious initial delay to any retail premium changes arising from the pool is from the flexibility given to insurers in choosing when and how to transfer eligible policies to the pool. However, even after joining, retail premium changes will take time to filter through to policyholders because:

- insurers will need to amend their pricing methodologies (see Section 5.2 for more detail) and implement these changes into their pricing systems
- existing policyholders will generally only realise the benefit of any changes on renewal, which could be up to 12 months after the insurer changes its pricing systems.

As discussed in Section 3.1, insurers can choose how to transfer their portfolios into the pool. For example, insurers may:

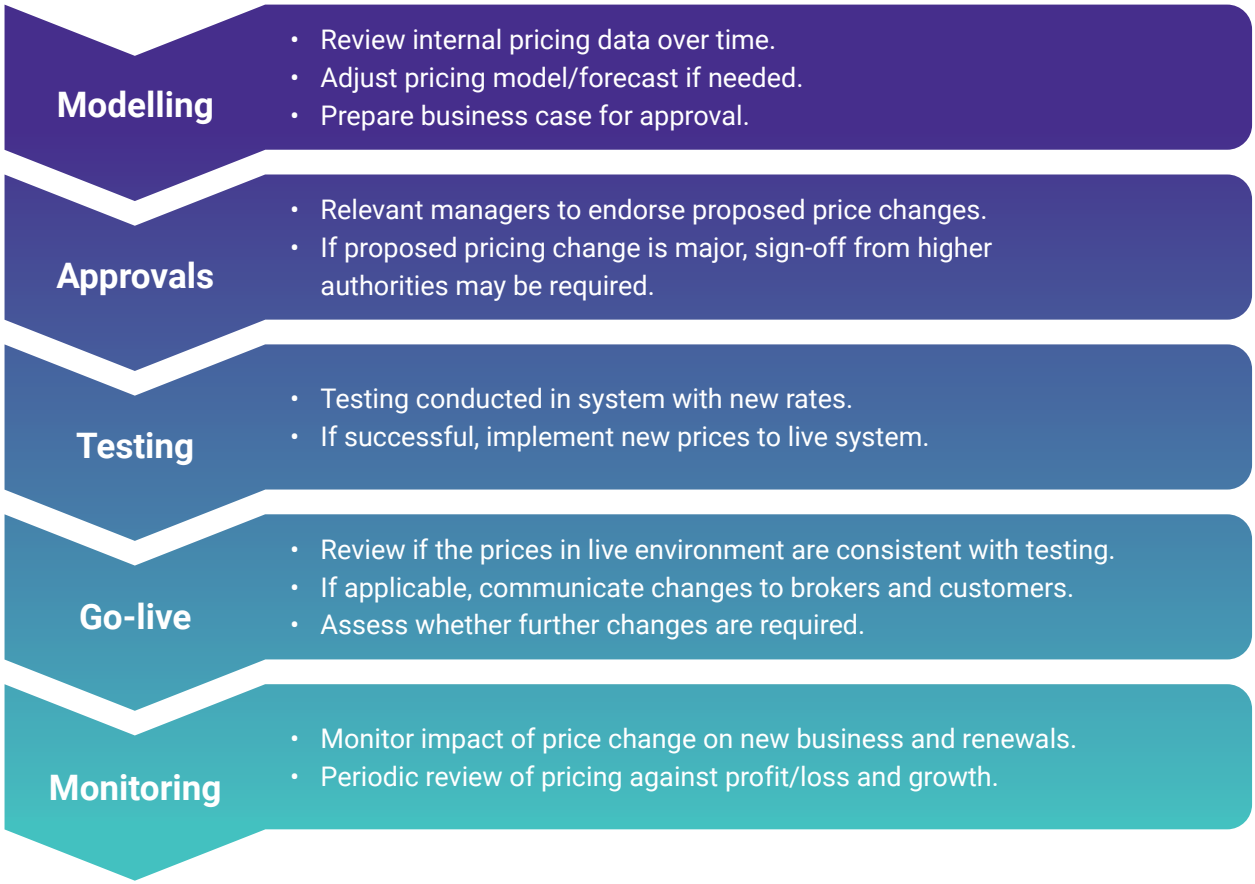
- choose a single bulk transfer of all eligible policies, or
- transfer by a progressive approach, whereby certain brands, or certain classes of eligible policies (such as householders first, followed by strata and SME),[234] are transferred at different times, as long as all eligible policies are transferred on or before the mandatory deadline.[235]

When and how an insurer plans to make changes to its pricing systems will also affect the timing of the pool's impact on a policyholder's individual premium. Making changes to a pricing system can take time and resources before the price change is applied to the relevant portfolio. Below is a simplified process for implementing a price change, based on the documentation we compelled from insurers.

234 Allianz, *Allianz joins the Cyclone Reinsurance Pool* [media release], Allianz, 16 March 2023, accessed 6 October 2023; Allianz, *Allianz Direct Home Insurance now available in new areas across Northern QLD and WA, after joining the Cyclone Reinsurance Pool* [media release], Allianz, 1 March 2023, accessed 30 October 2023.

235 QBE, *The Cyclone Reinsurance Pool explained – what's changing and why* [media release], QBE, 27 July 2023, accessed 6 October 2023.

Figure 5.2: Generic price change process



The time and difficulty involved in processing a retail price change following entry into the pool differs significantly among insurers. One insurer anticipated taking up to 6 months to develop and incorporate the pool's requirements into its pricing and analytics strategy. The insurer then proposes to observe any trends in its key metrics over a 12 to 18-month period to ensure it has achieved its pricing strategy following these changes. Another insurer expects its new pricing to be effective approximately 4 months after entering the pool.

Some insurers plan to undertake an iterative approach with how they change their retail prices with regards to the pool. For example, one insurer planned to use a staggered approach to updating its pricing, starting by reconfiguring its prices prior to entering the pool. It subsequently intends to analyse its retained loss and peril reinsurance costs some months after entering the pool, which it noted may result in a need to adjust its premium ratings.

Once the required changes have been made to an insurer's pricing engine, the pricing change will generally be reflected in premiums charged for new customers or on renewal for existing policies. For most policyholders who pay their insurance premiums annually, this means there could be a delay of up to 12 months before an existing policyholder will experience any benefit of the pool. For example, Allianz transitioned its eligible home and contents, and landlord policies into the pool by 1 January 2023. It stated that premium changes will come into place for any relevant policies that are entered into or renewed with an effective date of 1 January 2023 onwards.[236] This means that existing policies that were renewed prior to 1 January 2023 will not observe these premium changes until the next renewal.

236 Allianz, *Allianz joins the Cyclone Reinsurance Pool* [media release], 16 March 2023, accessed 26 July 2023.

The combination of insurers joining the pool at different times, the time required to implement pricing changes, and policy renewal cycles collectively mean that, even though many large insurers have joined the pool, policyholders may not see the pool's impact in their insurance premiums for quite some time.

The above observations around timing, in combination with how the pool is designed, particularly those elements that enable insurer discretion in their approach to and timing of entry to the pool, also highlight the complexity of monitoring the impact of the pool. Accordingly, we are unable to provide a clear picture of the impact of the pool at this time. Over the course of our monitoring role, we will continue to focus on identifying any savings resulting specifically from the pool, whether savings get passed on to policyholders; including identifying the spectrum of outcomes for policyholders that may arise from the different implementation approaches insurers have used.

6. Availability of insurance

Whilst the price of insurance is the focus of the ACCC's monitoring work, it is important to consider price alongside consumers' concerns about the availability of insurance. Some individual consumers may be unable to find any insurer willing to offer insurance for their property, while for other consumers, there is a perception of lack of availability because the only options available are prohibitive in cost. Both scenarios are significant and, in a practical sense, may be difficult to separate.

For consumers in northern Australia, the availability of insurance can depend on their specific region and risk profile. Access by insurers to more data to inform risk assessments and more complex pricing models has enabled them to set premiums with reference to an increasing range of consumer and property characteristics. Insurers can, and do, selectively target certain locations and/or types of risk, based on this data, which affects availability for potential customers.[237] In addition to using price to manage exposure (see Chapter 4), insurers can also use a range of other strategies to more directly limit the supply of insurance in areas they perceive to be risky, such as embargoes, exposure limits and other restrictive underwriting guidelines.

Data we collected from insurers this year has confirmed that home, contents, strata and small business insurance markets across northern Australia are generally serviced by at least a small number of insurers, ranging to many insurers in other regions. However, there are also regions of northern Australia for which markets appear to be much more concentrated. This is consistent with concerns that continue to be raised with us by local communities about the lack of choice they face compared to consumers elsewhere in Australia. Further, there may be individual properties within these regions for which insurers are not willing to offer insurance at all, and in this sense, the data we collect and present in this chapter does not represent the lived experience of every individual consumer.

The pool is designed to improve the availability of insurance by reducing insurers' exposure to the higher and more volatile claims costs for cyclone events, thus reducing one potential barrier for entry or expansion in northern Australia. The ACCC has previously found there are a range of other barriers also affecting these markets. These may continue to be present, despite the effects of the pool.

This chapter has 4 sections:

- First, we discuss potential barriers to entry and expansion into northern Australian insurance markets which may impact availability of insurance (Section 6.1).
- Second, we provide an overview of common underwriting restrictions that insurers use to manage risk exposure that can impact availability (Section 6.2).
- Third, we consider how the pool might influence availability of insurance in cyclone-prone regions (Section 6.3).
- We then look at insurers' presence in cyclone-prone regions as of September 2022 (Section 6.4).

6.1 Insurers may face barriers to expanding into northern Australia

The ACCC continues to hear from consumers in northern Australia that they lack choice of insurers and want to see more insurers active in local markets. We have also heard proposals from

237 ACCC, *NAII final report*, pp 135–137.

stakeholders that insurers should be *required* to offer insurance in northern Australia.[238] There are currently no such conditions requiring insurers who supply insurance in one part of Australia to also supply insurance in northern Australia as part of obtaining a license from APRA to supply insurance in Australia.[239]

As part of the Northern Australia Insurance Inquiry, we engaged with Australian insurers *not* active in northern Australia at the time of that inquiry to better understand what they perceived as barriers to their expansion (or re-entry) into northern Australian markets.[240]

At that time, we found that the most significant challenges for potential new entrants to northern Australia stem from the volatility and higher risk profile of the region. We found this gives rise to barriers including:

- an increased capital requirement and/or dependence on reinsurance to meet higher and more volatile claims costs
- the need to obtain and augment the risk data necessary to price with confidence (placing new entrants at an initial competitive disadvantage compared to participants with local knowledge)
- the costs of establishing or expanding builder and repairer networks (especially in remote regions and at times of peak demand)
- obtaining sufficient scale (because of population density and geographical spread, sub-regions of northern Australia can have relatively small premium pools).

While we observed the importance of reinsurance in northern Australia, where claims costs are more variable and subject to major spikes resulting from catastrophe events, access to reinsurance was not, at that time, identified as a significant barrier to expansion or re-entry into that region. However, insurers were conscious of the incremental reinsurance premium impact of supplying insurance in higher risk areas.

As part of the Northern Australia Insurance Inquiry, we also considered the merits of requiring insurers to supply insurance in northern Australia.[241] While such a measure has the potential to lead to more insurers offering insurance in northern Australia, and potentially greater competition for some consumers, we considered that the likely detriments of such a measure would outweigh the potential benefits.

Similar to the barriers to entry we found more generally, we found that licence conditions or authorisations requiring supply in all geographic regions could further raise barriers by placing smaller insurers, who may not already be active in northern Australia, at a disadvantage. As such, it could act as a disincentive for new insurers to enter the Australian market altogether. This is because insurers would need to rely on industry hazard and claims history data, which may not be of sufficient detail to appropriately understand and price policies in particular regions of northern Australian. Further, insurers who do not currently have a presence in northern Australia could face difficulty attracting consumers, especially where consumers face high search costs and information problems.

In addition to these concerns, the Northern Australia Insurance Inquiry also found a number of significant implementation challenges with such a measure, particularly with regard to determining the amount of business (however measured) that an insurer should be required to have in any particular target area (the 'quota level'). Regardless of how a quota was set, insurers would need a reasonable amount of time to adjust their operations in order to be able to meet it, especially where an insurer had little or no presence in a market.

238 For example, Townsville Chamber of Commerce, *Submission to the Joint Select Committee on Northern Australia: Inquiry into the cyclone reinsurance pool*, 2022, accessed 13 November 2023. See also *NAII final report* 2020, p 190–191.

239 General insurers are required to be authorised under the *Insurance Act 1973* (Cth) and once licensed by APRA, they are subject to prudential supervision. This licence is required before an insurer can supply the relevant products in Australia.

240 ACCC, *NAII final report*, Chapter 11.

241 ACCC, *NAII final report*, pp 190–192.

In part, the government established the pool with the aim of improving access to insurance for home, strata and small business consumers in cyclone-prone regions by improving the availability and reducing the cost of reinsurance. This is intended to encourage insurers to expand their products in areas of high cyclone-related risk. In Section 6.3, we consider how the pool may facilitate this in more detail.

6.2 Why and how insurers manage their exposure to risk

Recent catastrophes in Australia have highlighted the potential impact on insurers of having a large number of customers in any given high risk geographic location which can result in significant claims costs if large scale damage occurs. Large exposures in catastrophe-prone areas also raises costs for insurers in the form of increased prudential capital requirements and reinsurance costs.[242]

In addition to using price to manage exposure, insurers can also use a range of other strategies to more directly limit the supply of insurance in areas they perceive to be risky, such as embargoes, exposure limits and other restrictive underwriting guidelines as explained below.

6.2.1 Exposure limits and embargoes

Insurers monitor their exposure to perils and in geographic areas, as well as their concentration risk, to ensure that they remain within the risk appetite of their business. Insurers also monitor exposure levels across all of Australia to ensure that they remain within the limits of their reinsurance programs and are able to purchase additional coverage if required.[243]

Insurers use a range of mechanisms to manage risks that they see as undesirable due to the potential for significant claims costs in the event of a catastrophe affecting the area. In addition to using premium adjustments to manage risk through price (as discussed in Section 4.3), they can also choose to not offer insurance to particular consumers at all. Embargoes, exposure limits and other restrictive underwriting guidelines, such as not insuring buildings over a certain age, are examples of mechanisms used by insurers to manage their risk exposure.

The application of restrictions on the supply of insurance may be a considered commercial decision for an insurer. However, it has the effect of limiting the availability, or choice, of insurance for consumers. To better understand the potential interaction between the pool and availability in cyclone-prone regions, we asked insurers for information on their use of exposure limits and embargoes for the period July 2021 to March 2023 (see Box 6.1 for an explanation of these underwriting restrictions). This information provides us with an overview of restrictions in place pre-pool and during its implementation.

242 ACCC, *NAII final report*, p 117.

243 ACCC, *NAII final report*, p 239.

Box 6.1: What are exposure limits and embargoes?

Exposure limits are a risk management tool used by insurers to cap the volume or proportion of customers or sum insured in a particular area.[244] For example, if an insurer decides to underwrite in high cyclone risk areas, in order to ensure it is maintaining appropriate levels of reinsurance coverage, it may limit the risks it is willing to underwrite to a certain dollar amount or percentage of its total aggregated exposure. Thus, while the use of exposure limits means some risks can be underwritten, it caps the overall availability of insurance to consumers.

Embargoes are a risk management tool used by insurers to restrict underwriting. This is where insurers place a restriction on writing new policies and/or not renewing existing policies in a specific area or for a specific peril, or both. For example, an insurer may consider that a high-risk bushfire location is outside of its risk appetite and, as such, implement an embargo that denies any underwriting for postcodes in this location. We refer to these as **ongoing embargoes** as they have no natural end point and will only be removed at the insurer's discretion.

There are also **event-based embargoes**. These are embargoes on underwriting new risk which are put in place for specific events. An insurer that uses these embargoes will stop underwriting for the predicted affected location of the event, such as postcodes in the path of a developing cyclone, and will remove that restriction when that event has passed.

Embargoes are different to a timed **exclusion period**, where there is a waiting period between when a policyholder purchases a new insurance policy and when they are insured under the policy for loss or damage caused by a particular event, such as storm, flood or fire. This exclusion period is usually up to 72 hours and will be set out in the Product Disclosure Statement for the policy.

Exposure limits may allow insurers to underwrite in riskier markets while still being within the overall risk strategy of their business. Exposure limits also assist insurers when they underwrite through a broker as this allows brokers to use their professional skills to bring in risks that are more aligned to the insurer's risk appetite. For example, one insurer does underwrite high risk cyclone regions in Queensland for its broker product but has a stated limit of 1% of portfolio sum insured aggregates.

The majority of insurers indicated to us that they do not explicitly apply exposure limits to their supply of insurance.

Conversely, we found that the majority of insurers we obtained information from use some sort of embargoes as part of their risk management strategy. This may partly reflect a relative ease for insurers of implementing embargoes into their offer and pricing engines and adding to online quotation systems, compared to exposure limits.

Insurers using embargoes are doing so in varied ways. The majority of insurers that use embargoes indicated to us that they implement embargoes on an ongoing basis. Insurers apply different criteria for their ongoing embargoes that consider a combination of location, perils and their overall risk appetite. For example, one insurer indicated that it has a 'decline' embargo on some postcodes. However, for other postcodes the same insurer applies embargoes only to the underwriting of certain perils, such as high flood risk, that are outside of its risk appetite.

Several insurers indicated that they use some form of event-based embargoes. Defense Service Homes Insurance explains to consumers on its website that it applies 'embargoes on new insurance

244 ACCC, *NAII final report*, p 146.

policies to restrict people buying insurance when the risks are viewed as highly elevated, or a disaster is already occurring, and then canceling cover after the risk passes'.[245]

In terms of granularity, most insurers apply embargoes at a postcode level. Only a few insurers indicated that they apply embargoes at the address level. If an insurer applies an embargo at an address level, it means that, for example, they may choose to offer insurance to consumers whose individual properties are at a lower risk of flooding in a postcode that would be considered high risk at the aggregate level.

Documents provided to us by several insurers indicated that they have a lack of risk appetite for underwriting selected products above the 26th parallel. Another insurer noted that it does not underwrite above the Tropic of Capricorn due to natural peril risks. How the pool may influence insurers' risk appetites is discussed in Section 6.3.

6.2.2 Challenges in strata insurance availability

The ACCC is aware of concerns of some strata residents across northern Australia about the challenges they are facing in being unable to find residential strata insurance from domestic insurers, or that they can only do so at a significantly increased premium compared to previous years. These concerns are not new but are being raised with us in the context of our monitoring role with a renewed sense of urgency.

State and territory legislation in each of Queensland, Western Australia and the Northern Territory imposes a legal requirement for strata titled properties to insure common property building and assets for their full replacement or reinstatement value.[246] Whilst the respective legislative requirements across these 3 jurisdictions differ slightly, it is a reasonable generalisation that there is a mandatory requirement for insurance to be held for strata properties. There are very limited exemptions to these requirements for full insurance, particularly in Queensland and Western Australia.

Aside from any private motivation from lot owners to seek insurance to cover their assets, this mandatory legal requirement to hold residential strata insurance adds to the pressure for strata residents (and the strata managers who represent them) to obtain adequate insurance in markets which may be very challenged by limited availability and/or very high prices.

In 2019, as part of the Northern Australia Insurance Inquiry, we undertook a detailed investigation of the particular challenges facing residential strata insurance.[247] At that time, we found that strata insurance availability concerns did not appear widespread, however, for a subset of strata properties in northern Australia, they can be severe. These properties tended to be large (over $5 million sum insured and over 10 dwellings); older (particularly for those built before 1985); and located in close proximity to the coastline, offshore islands, or in very remote postcodes.

In addition, we found that strata availability for a subset of properties had worsened over the course of that inquiry, with a number of insurer intermediaries tightening their underwriting criteria in cyclone regions in northern Australia for properties of certain construction types (such as walls that are not 100% brick or concrete and properties with tiled roofs) and a recent claims history.

The intermediated nature of strata insurance markets also impacts strata insurance availability, with the Northern Australia Insurance Inquiry finding that commission arrangements can give rise to

245 Australian Government, Department of Veterans' Affairs, *Embargo FAQs*, DSH website, n.d., accessed 15 November 2023.

246 For WA, *Strata Titles Act 1985* (WA) section 97 and Schedule 2A, clause 53D; For QLD, *Body Corporate and Community Management (Standard Module) Regulation 2008* (Qld) sections 178–180; For NT, *Unit Title Schemes Act 2009* (NT) sections 52–54, and *Unit Titles Act 1975* (NT) section 80.

247 ACCC, *NAII final report*, p 390.

brokers and strata managers including insurance providers' remuneration arrangements as part of their selection criteria for choosing an insurer.[248]

Concerns raised with the ACCC this year from individual strata residents and local community representatives, particularly in north Queensland, suggests that strata insurance remains a significant concern, at least for some types of strata. One insurer indicated that its lack of risk appetite for insuring strata risks in northern Australia is due to a range of factors such as their remote/regional location, low sums insured, inferior construction quality, limited access to public water supply and fire and security protection, and limitations on its (i.e. the insurer's) ability to assess and service claims in these regional areas.

We will continue to closely monitor strata availability challenges over the course of this monitoring role. In particular, we will look to shed more light on the classes of properties that are more acutely affected and the extent to which the commencement of the pool impacts the availability of strata insurance.

Alternative insurance arrangements

The vast majority of residential strata properties in Australia are insured under residential strata insurance products distributed by domestic insurers. However, alternative insurance arrangements exist for properties experiencing difficulties in obtaining residential strata insurance market. In particular, properties may obtain cover via an Industrial Special Risk (ISR) policy from either domestic or international insurers, or may seek insurance from the Lloyd's of London market, colloquially known as Lloyd's.

Box 6.2: Industrial Special Risk (ISR) policies and Lloyd's of London

Industrial Special Risk insurance is a broad property cover product typically for high value business assets, generally valued at $5 million or more. ISR products are generally designed for commercial assets, and often includes consequential loss or business interruption cover which exceeds the requirements of insurance for many residential strata properties.

Lloyd's of London is a specialist insurance and reinsurance market that provides underwriters for general insurance products. Around the world (as at 31 December 2022), Lloyd's consists of 52 insurance companies (also known as managing agents), over 384 registered brokers and a global network of approximately 3,464 coverholders (also known as underwriters) who operate and underwrite the Lloyds market.[249] Lloyd's are licensed to operate in Australia and are regulated by APRA.

ISR policies tend to be policies of last resort, as premiums are more expensive and the coverage offered is more suited to properties with a business or commercial component.[250] At the time we undertook the Northern Australia Insurance Inquiry, the ACCC formed the view that the use of ISR policies to insure residential strata properties in northern Australia was limited, and used primarily by large, higher value strata properties. While we consider that it is likely the majority of residential strata properties in northern Australia are insured under residential strata insurance products distributed by domestic insurers, some strata residents in north Queensland are telling us of increased experiences with buildings resorting to ISR policies purchased from international insurers. These residents express strong concern about needing to resort to this option.

248 ACCC, *NAII final report*, p 394.

249 Lloyd's, *How the market works – Business at Lloyd's in still conducted face-to-face, and the bustling underwriting room is central to the smooth running of the market*, Lloyd's website, n.d., accessed 27 September 2023.

250 ACCC, *NAII final report*, p 395.

In a 2022 Strata Community Association survey of strata managers (in Australia and New Zealand), around 11% said they managed schemes with insurance outside Australia and New Zealand due to several reasons, such as inability to receive a quote from local insurers, general lack of availability or more competitive premiums in overseas markets.[251]

The Northern Australia Insurance Inquiry found that, similar to ISR policies, Lloyd's schemes appear to be used as an insurer of last resort. The premiums offered through Lloyd's schemes are more expensive and the coverage is more suited to risks which require a tailored insurance policy. One broker noted to that inquiry that Lloyd's had premiums that 'sting you' and, similar to ISR policies, the premiums charged tend to exceed rental income.

Whilst we are unable to collect data on all insurance policies sold by international insurers to Australian consumers, we remain interested to understand the extent to which this is occurring and will consider this issue further.

6.2.3 Challenges in small business insurance availability

There are significant challenges faced by small businesses when attempting to access insurance. The small business insurance market has a number of different characteristics compared to household and strata markets, with different operating insurers and a more intermediated market. However, similar to household and strata, the challenges in insurance availability for small business will not be simply alleviated by the pool taking on cyclone-related risk exposure.

The main challenges to availability in the small business market appear to relate more to the industry within which the business operates than its cyclone risk. In information provided to us, some small business insurers indicated that their risk appetite for underwriting small business products is limited to certain industries.

In 2020, the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) conducted an inquiry into insurance for small business, underpinned by concerns about availability and affordability of various types of insurance which thousands of small businesses are required to hold to legally operate. In relation to natural disaster insurance, the ASBFEO found that businesses reported being unable to obtain natural disaster insurance, or being offered policies where the cost is prohibitive. For some sectors, particularly rural pubs and regional accommodation businesses, ASBFEO found that property insurance is almost impossible to obtain. For other sectors, property insurance can be obtained but is so expensive as to be inaccessible, excludes key natural perils or has an excess so high the insurance is useless. As part of this inquiry, the ASBFEO recommended that the ARPC should be expanded to provide reinsurance for all natural disasters for commercial property insurance.[252]

Accordingly, regardless of the impact of the pool, it may be that the occupation risks driving coverage availability issues will remain for certain small businesses. Moreover, and again similarly to home and strata, we note, as found by the ASBFEO, that 'for many small businesses it is not possible to separate affordability of insurance from availability, as there is a price at which the insurance may as well not be available for purchase.'[253] We consider small business retail premiums in Chapter 9.

The ASBFEO inquiry examined issues broader than natural disaster risk, highlighting a range of issues around availability of insurance more generally. These include businesses that were unable to obtain insurance based on industry (such as the mining industry), location (such as remote locations) or

251 Strata Community Association, *A data driven holistic understanding of strata insurance in Australia and New Zealand*, Strata Community Association website, June 2021, accessed 25 August 2023.

252 Australian Small Business and Family Enterprise Ombudsman (ASBFEO), *Insurance Inquiry Report December 2020 [PDF 1,434KB]*, 10 December 2020, accessed 08 September 2023.

253 ASBFEO, *The Show Must Go On* [media release], December 2021, p 12, accessed 08 September 2023.

other generic factors.[254] The ASBFEO also touched on other issues impacting availability for small business insurance, such as public liability and professional indemnity insurance which are not covered by the pool.[255]

Affordability challenges were further highlighted in a subsequent 2021 ASBFEO report into insurance issues for Australia's amusement, leisure, and recreation sector, where the ombudsman stated that 'without the statutorily and contractually required insurance coverage [such as public liability insurance], the businesses in this sector will be unable to operate. This will lead to regional, rural, and metro shows, school fetes, carnivals and other events, being unable to offer rides and sideshow alleys, significant job losses, and stranded assets'.[256] Again, it is not (primarily) the geographical location of these small businesses that are of issue, as they are either mobile and/or spread across the country. Instead, the industry type presents a risk that insurers may deem to be outside their risk appetite, limiting availability of insurance for consumers. This is further discussed in Section 4.2.1, where we discuss how small business insurance premium calculations are more heavily influenced by working claims over natural peril claims.

6.3 How the pool is designed to encourage more availability

The government established the pool with the aim of improving access to insurance for home, strata and small business consumers in cyclone-prone regions. It does this by covering all eligible claims arising from cyclone and cyclone-related flooding events.[257] This, in turn, could help alleviate insurers' concentration risk concerns in these cyclone-prone areas by lowering their exposure to catastrophic loss as a result of a cyclone (concentration risk is outlined in Section 4.3.1).

It is too early to determine the extent to which the pool will motivate insurers to change their risk appetites and impact the availability of insurance. However, we have noted certain encouraging developments for consumers in cyclone-prone areas.

The pool has the potential to improve insurance availability by allowing insurers to remove cyclone-based risk selection from their underwriting restrictions. For example, once it entered the pool in January 2023, Allianz announced that it was removing embargoes in place on selected products in high cyclone risk postcodes, allowing consumers in these postcodes to seek quotes from the insurer.[258, 259] It is too early to observe the extent to which this has led to increased take up of Allianz policies in practice, but we will be able to observe this over the course of our monitoring role.

However, the pool may not, on its own, necessarily motivate all insurers to expand their supply of insurance to cyclone-prone regions. As discussed below, insurers may not currently be intending to expand their supply for a range of reasons, such as the ongoing need to obtain private reinsurance for risks not covered by the pool, the prevalence of other natural perils more generally, and/or an established preference not to serve high-risk cyclone regions.

Any proportion of claims that fall outside of the scope of the pool may require insurers to obtain reinsurance from the private market. An example of this is any expected claims after the 48-hour coverage period following the downgrade of a cyclone, which is discussed in Section 5.2.1. This risk

254 ASBFEO, *Insurance Inquiry Report December 2020 [PDF 1,434KB]*, p 25.

255 ASBFEO, *Insurance Inquiry Report December 2020 [PDF 1,434KB]*, p 21.

256 ASBFEO, *The Show Must Go On* [media release], December 2021, p 12, accessed 8 September 2023.

257 ARPC, *Insurer Onboarding*, ARPC website, n.d., accessed 1 September 2023.

258 Allianz, *Allianz Direct Home Insurance now available in new areas across Northern QLD and WA, after joining the Cyclone Reinsurance Pool* [media release], Allianz website, 1 March 2023, accessed 01 September 2023.

259 Allianz noted it may have a 72 hour exclusion period in place for certain weather events. *Allianz Direct Home Insurance now available in new areas across Northern QLD and WA, after joining the Cyclone Reinsurance Pool* [media release], Allianz, 1 March 2023, accessed 01 September 2023

outside of the pool may mean that insurers still employ embargoes and exposure limits in order to lower their other reinsurance costs, especially for insurers that use event-based embargoes.

In addition, insurers may not be motivated to lift embargoes or raise exposure limits due to other factors which they consider in assessing whether or not to offer insurance, such as the characteristics of a particular building or its risk of damage from non-cyclone natural perils. Insurance availability can be influenced by various factors that may mean broad embargoes on underwriting any risk, such as those above the 26th parallel outlined in Section 6.2.2, may still be utilised despite the pool.

For example, in assessing the impact of other natural perils, one insurer noted that its average annual loss of its portfolio was predominantly affected by the February 2022 flood that hit South-East Queensland and northern New South Wales. In response to that severe weather event, the insurer changed its flood acceptability criteria in the Brisbane river area and increased its flood base rates. The pool will not cover flood risk outside of cyclone-related flooding, meaning that there may remain significant natural perils that impact insurers' willingness to make insurance available in areas identified as 'cyclone-prone'.

As previously mentioned, it is still too early to tell if insurers will be removing embargoes on high cyclone risk regions as a result of the pool. One insurer noted concern that the proposed premium rates (of the pool) will not create savings for its existing customers due to its existing low exposure to high-risk cyclone areas. However, the same insurer also noted that:

> Should the pool not fully compensate the additional risk that we would take in writing potential business in northern Australia, then this would compromise our competitiveness (and therefore affordability) for our customers. However, for strategic reasons, should we decide to write business in the tropics in the future, the pool in theory should make writing this business more feasible.

Another insurer indicated that it expected the pool would have minimal impact for some insurance products due to its existing embargoes in high-risk cyclone areas.

In future reports, we will monitor if the pool has led to further changes to insurer risk management practices that affect availability.

6.4 Availability of insurance in cyclone-prone regions

We obtained data from insurers for policies in effect as at 30 September 2022.[260] The insurers we collected policy level data from include the 14 largest direct general insurers in Australia by gross written premium for the financial year ending 30 June 2023.[261]

In this section, we present the number of insurers from our sample with more than 10 insurance policies of different product types in effect by region, to see the broad insurer presence in northern

260 We have used policy level data to measure the number of insurers with policies in effect by region or postcode of the insured property. There may be insurers offering policies that did not have any policies in effect as at the reference date, or other insurers offering these types of policies that we have not collected policy level data from. Because we have focused our collection of policy level data on insurers that will be joining the pool, it is likely that the number of insurers in regions outside of Northern Australia is greater than presented in this analysis. We note that the numbers of insurers presented in this analysis is greater than the number of insurers analysed in the Northern Australia Insurance Inquiry. Further information on our methodology is provided in Appendix A.

261 APRA, *Statistics – Quarterly general insurance institution-level statistics database from September 2017 to June 2023*, 24 August 2023, accessed 15 November 2023.

Australia compared to the rest of the country. We have also selected certain population centres to examine more closely.[262]

Our data shows that, overall, a number of insurers are supplying home, strata and small business insurance in most regions of northern Australia. However, this aggregated result disguises that there may be individual properties within these regions for which insurers are not willing to offer insurance at all (or only at a price which is unaffordable). Accordingly, the data we collect and present does not represent the lived experience of all individual consumers. We will extend this data to later time periods and consider ways to further examine availability in future reports.

As discussed in Section 6.2.1, insurers may use a combination of location, susceptibility to perils and their overall risk appetite to decide whether they will write a policy. An insurer's presence in a region also does not mean that policies offered or written in that region will be affordable for consumers. Insurers may use price to manage their risk exposure (as discussed in Chapter 4) rather than directly limiting the areas they write policies in.

Table 6.1 below shows the number of insurers with more than 10 home, strata or small business insurance policies in effect by region. The table indicates that the 'rest of Australia' had the most insurers out of these northern regions, but not substantially more than any northern Australia region. The Northern Territory had the fewest insurers for home, north Western Australia had the fewest for strata, and both of these regions had the fewest for small business.

Table 6.1: Number of insurers with more than 10 home[263], strata or small business[264] insurance policies in effect, by region, 2022

Region	Home and/or contents insurance	Strata insurance	Small business insurance
North Western Australia	10	3	7
Northern Territory	7	4	7
North Queensland	12	7	9
Rest of Australia	13	7	10

Source: ACCC analysis of data provided by insurers.

Across all regions, there were generally less insurers with strata and small business policies in effect as compared to insurers with home insurance policies in effect. This could partially be due to the scope of policies we have collected data for.[265] However, it is not surprising that there are more insurers supplying home insurance products, given the relative size of that market. For example, recent statistics from IBISWorld indicate that, other than motor vehicle insurance, home insurance was the largest Australian general insurance category in terms of 2023 revenue.[266] Furthermore, within Australian home and contents insurance revenue in 2023, strata insurance only accounted for 19.4%.[267]

262 Policy level data has been grouped using a combination of low-resolution CRESTA Zones and high-resolution CRESTA Zones, mapped by postcode as a proxy, to show the select towns and cities. CRESTA Zones are used by the insurance and reinsurance industry for the technical management of natural catastrophe insurance. CRESTA, *CRESTA* [website], n.d., accessed 7 September 2023.

263 'Home insurance' includes combined home and contents, home only and home contents only insurance policies.

264 'Small business insurance' includes combined small to medium enterprise (SME) building and contents, SME building only, SME contents only and SME business interruption insurance policies.

265 We have focused our data collection on policies that may be covered by the pool. Policies that are categorised as strata insurance are limited to those where 50% or more of the total floor space is used wholly or mainly for residential purposes. Small business insurance policies we have collected data for are limited to those where the total sums insured do not exceed $5 million. Further information on our data collection and methodology is provided in Appendix A.

266 IBISWorld, *General Insurance in Australia – Products and Markets*, IBISWorld website, n.d., accessed 23 August 2023.

267 IBISWorld, *General Insurance in Australia – Products and Markets*, IBISWorld website, n.d., accessed 23 August 2023.

It is important to note that insurers often supply insurance via multiple brands and intermediaries, allowing them to target consumer segments with differentiated pricing and policy coverage options. This can provide another competitive dimension and may have positive outcomes for consumers. However, it has equally been described as an 'illusion of competition' and adds another level of complexity for consumers in trying to compare between different underwriters who may have different views of risk.[268] Multiple brands and insurer intermediaries may result in a consumer comparing a greater number of brands but fewer insurers if they are not aware of which insurer underwrites each brand. It also adds to search costs as it greatly increases the number of potential policies for a consumer to compare.[269]

6.4.1 Home insurance

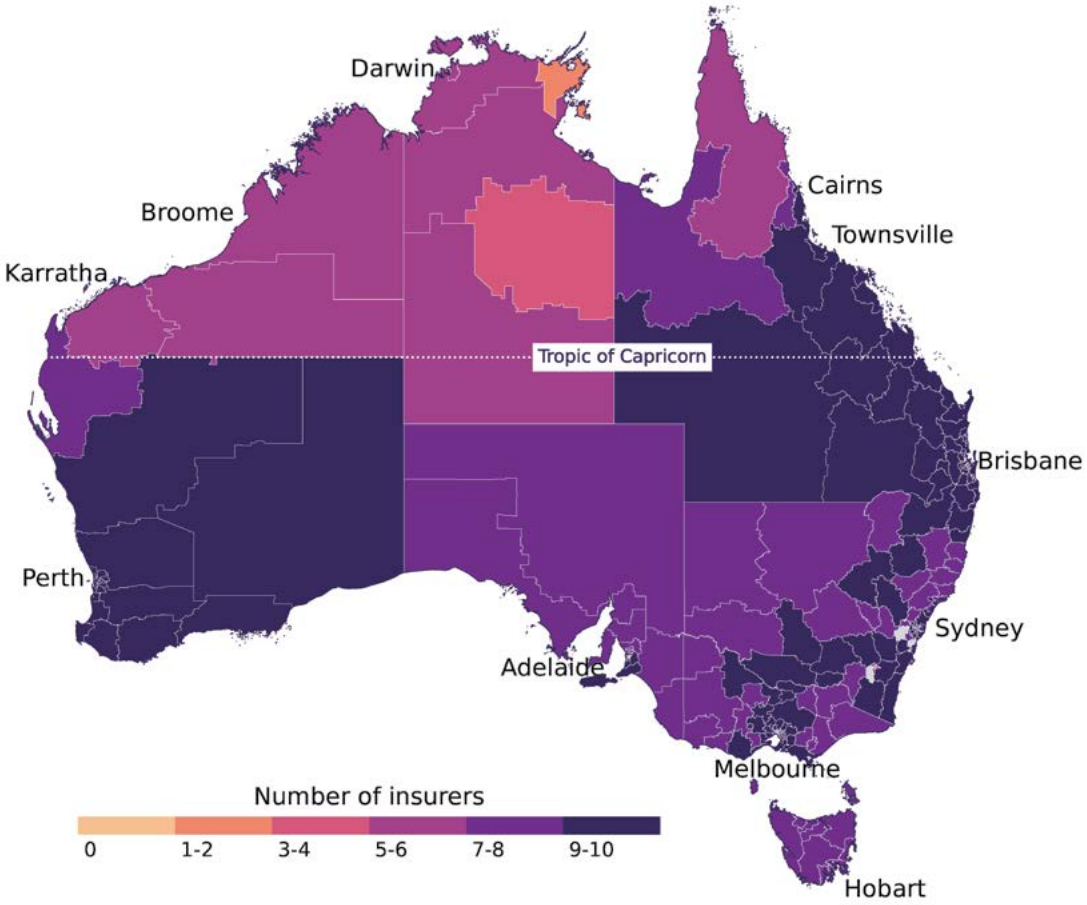
Figure 6.1 below shows the number of insurers with more than 10 combined home and contents policies in effect around Australia.[270] As can be seen by the darker shading on the map, many regions of Australia had at least 9 insurers with policies in effect. Regions with fewer insurers tended to be in the northern regions of Australia. Of the northern Australian regions, north Western Australia broadly had 6 or less insurers, as did the Northern Territory. North Queensland had regions with at least 9 insurers, but the number of insurers decreased as we looked further north, where there were areas with 6 or less insurers.

268 Senate Economics References Committee, *Australia's general insurance industry: sapping consumers of the will to compare*, Parliament of Australia website, n.d., accessed 4 September 2023.

269 ACCC, *NAII final report*, p 138.

270 As at the reference date by Statistical Area Level 3. Statistical Areas Level 3 (SA3s) are geographical areas that have been designed for the output of regional data. Australian Bureau of Statistics, *Statistical Area Level 3*, Australian Bureau of Statistics website, accessed 7 September 2023.

Figure 6.1: Number of insurers with more than 10 combined home and contents insurance policies in effect, by Statistical Area Level 3, 2022

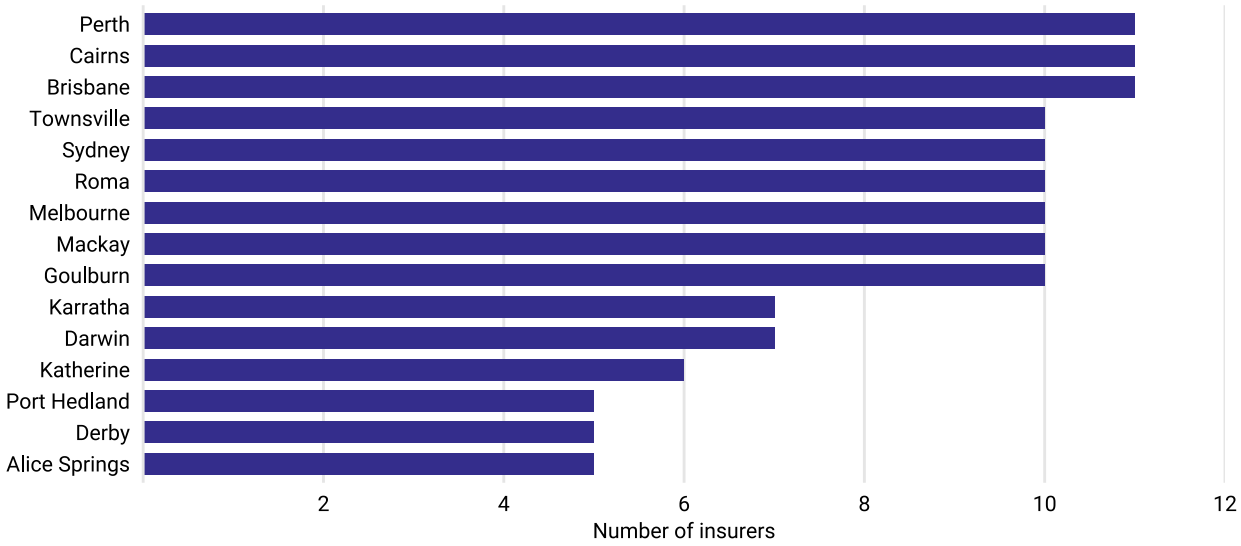


Source: ACCC analysis of data provided by insurers.

Note: The small grey areas on the map indicate insufficient data. Geographically smaller Statistical Area Level 3 regions may not be clearly visible on the map.

Figure 6.2 below shows the number of insurers with more than 10 combined home and contents, home only, or home contents only insurance policies in effect by select towns or cities. Of the cities and towns we looked at individually, Alice Springs, Derby and Port Hedland had the fewest insurers with policies in effect, at 5 insurers. These towns with the fewest insurers are all located in northern Australia, but there are also cities and towns in northern Australia such as Townsville and Mackay with a comparable number of insurers with policies in effect to capital cities such as Melbourne and Sydney, all of which had 10 insurers from our sample. This suggests that most relatively large cities or towns have a number of insurers, but that availability issues are starker outside of the regional centres.

Figure 6.2: Number of insurers with more than 10 home and/or contents insurance policies in effect, select cities and towns, 2022



Source: ACCC analysis of data provided by insurers.

As noted, despite an insurer's broad presence in an area, the methods they use to determine whether they will write policies (as discussed in Section 6.2.1) can mean a different experience of insurance availability even within a city, based on the individual characteristics of the property for which insurance is sought. Another key factor to consider in this context is the price of insurance (the prices of home insurance are discussed in Section 7.1).

6.4.2 Strata insurance

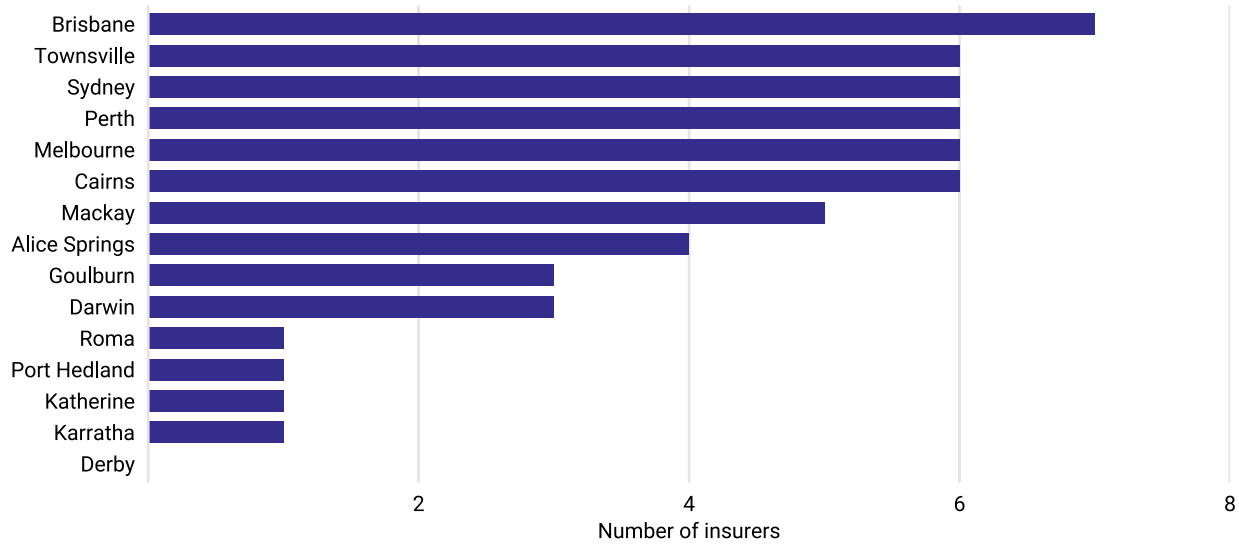
Figure 6.3 below shows the number of insurers with more than 10 strata insurance policies in effect by town or city. There is wide variation between these regions in the number of strata insurers. Areas of north Western Australia had very few insurers, such as Derby with no insurers that had more than 10 strata insurance policies, and Karratha and Port Hedland with one insurer each. Areas of the Northern Territory similarly had few present insurers for strata, Katherine only had one insurer while Darwin had 3. There may however be very few strata title properties in a number of these regions, meaning there would be limited demand for strata insurance and hence limited strata insurance policies in effect.

Other than capital cities, areas in north Queensland had the most strata insurers from our sample out of the select towns or cities, with 6 insurers in Townsville and Cairns, and 5 in Mackay. Contributing to the higher numbers in these regions may be recent entrant Sure Insurance Pty Ltd which only writes insurance in Queensland[271] and RACQ Insurance Limited which predominantly writes strata insurance in Queensland.[272]

271 Sure Insurance, *About*, Sure website, accessed 23 August 2023.

272 RACQ Insurance Limited, *RACQ response to exposure draft legislation and regulations [PDF 4.5MB]*, p 7, accessed 15 November 2023.

Figure 6.3: Number of insurers with more than 10 strata insurance policies in effect, select cities and towns, 2022



Source: ACCC analysis of data provided by insurers.

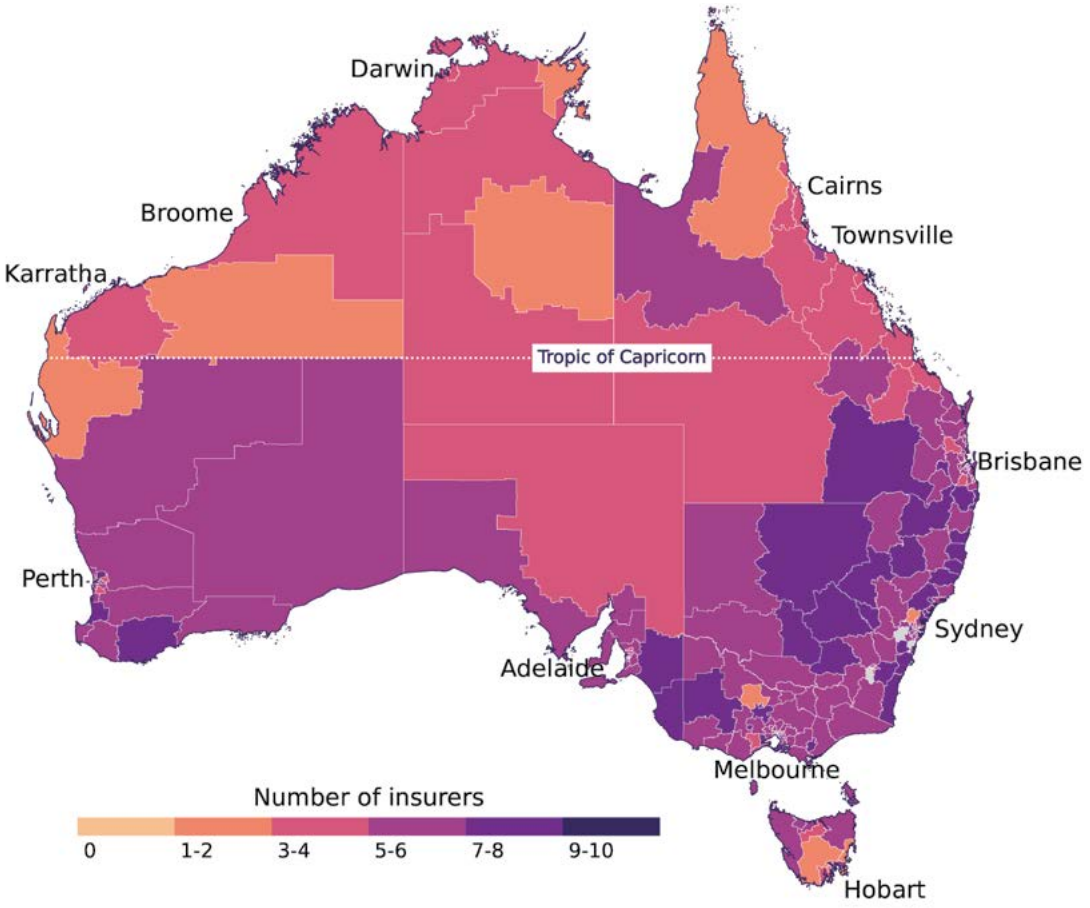
While the above availability figures indicate there are a number of insurers offering strata policies in northern Australia, the number of insurers is notably fewer than for household insurance. The availability is also often highly region-specific. In response to the 2022 Strata Community Association survey, some strata managers said that local specialist insurers refused to cover specific areas such as the Pilbara, north Queensland and other particular regions.[273] Even in areas with multiple insurers, availability concerns can be severe for particular strata properties (as discussed in Section 6.2.2). In addition to whether an insurer is present, multiple factors other than location can impact strata insurance availability including building age, construction material, and previous claims history. A combination of these factors and the location of the insured property can result in very high prices (see Section 8.1 for more information about strata insurance prices) or quote refusals for strata title properties.

6.4.3 Small business insurance

Figure 6.4 below shows the number of insurers with more than 10 combined small business building and contents insurance policies in effect across Australia. The map illustrates a moderate number of insurers with small business policies in effect in regions surrounding capital cities. There are various lighter areas on the map indicative of having few insurers, particularly in regions of northern Australia.

273 Strata Community Association, *A data driven holistic understanding of strata insurance in Australia and New Zealand*, Strata Community Association website, June 2021, accessed 25 August 2023.

Figure 6.4: Number of insurers with more than 10 combined small business building and contents insurance policies, by Statistical Area Level 3, 2022

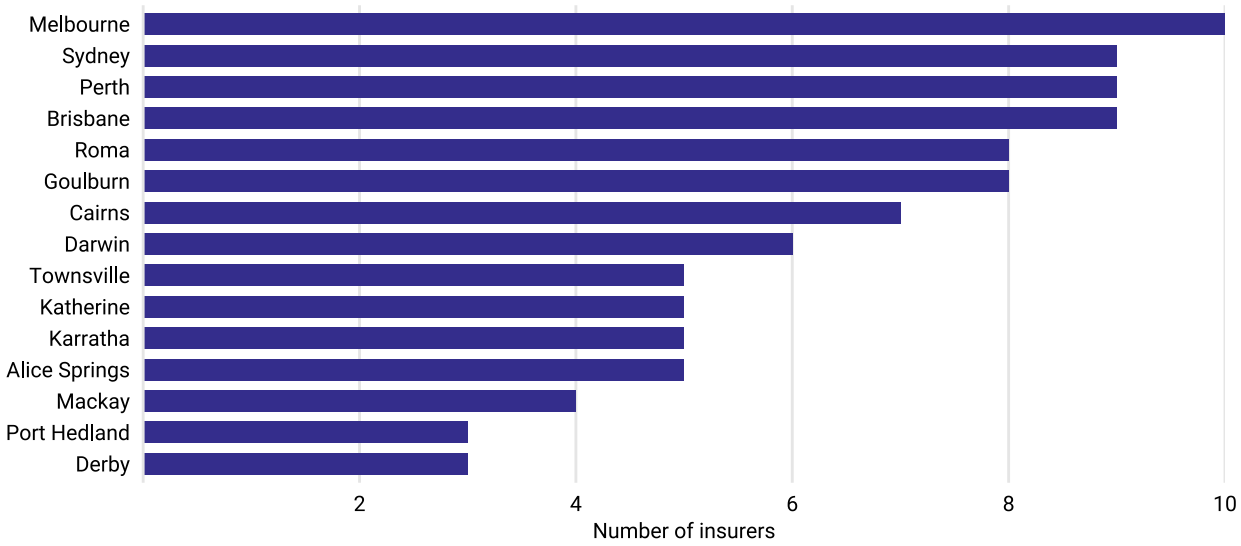


Source: ACCC analysis of data provided by insurers.

Note: The small grey areas on the map indicate insufficient data. Geographically smaller Statistical Area Level 3 regions may not be clearly visible on the map.

Figure 6.5 below shows the number of insurers with more than 10 combined small business building and contents, small business building only, small business contents only, or small business interruption insurance policies in effect by town or city. There tended to be less insurers from our sample with small business policies in effect in areas in northern Australia than in the rest of Australia. For instance, Melbourne had 10 insurers which was the most, followed by Sydney, Perth and Brisbane with 9 each. Derby and Port Hedland only had 3 insurers which was the least.

Figure 6.5: Number of insurers with more than 10 small business insurance policies[274] in effect, select cities and towns, 2022



Source: ACCC analysis of data provided by insurers.

Fewer insurers in the regional areas is consistent with findings in ASBFEO's Small Business Insurance Inquiry that businesses were reporting being unable to obtain insurance in remote locations. Businesses also reported being unable to obtain natural disaster insurance, or only being able to obtain property insurance that excludes key natural perils or was otherwise unaffordable. Other challenges in small business insurance availability are discussed in Section 6.2.3 and the prices of small business insurance are discussed in Section 9.2.

274 'Small business insurance' includes combined SME building and contents, SME building only, SME contents only and SME business interruption insurance policies.

7. Home insurance

Consumers across northern Australia continue to raise concerns with the ACCC about their experiences of high and rising home insurance premiums. Some shared their examples of renewal notices in the order of hundreds and sometimes thousands of dollars more than the previous year. A key objective of the pool is to help make home insurance premiums more affordable for consumers at high risk of cyclones.

In this chapter we look at the prices and a breakdown of premiums for home insurance, focusing on combined home and contents insurance. In Section 7.1, we examine the premiums paid for combined home and contents insurance by different regions and over time. We also analyse average premiums by sum insured, average premiums by excess, and average premiums by excess and sum insured, in order to provide more standardised comparisons. In Section 7.2, we look at a breakdown of retail premiums into the various components that contribute to the insurance premiums charged to the policyholder.

The figures presented in this chapter show information up until 30 June 2023. As only a few insurers had joined the pool at this time, our analysis of the pool's effect is necessarily limited. We anticipate being able to present more direct analysis of the pool's effect in future reports once a greater number of insurers have been in the pool for a longer period.

Chapters 8 and 9 provide equivalent analysis for strata and small business policies.

We used our information gathering powers to obtain policy level data, policy and claims summary information and financial information from select insurers. These collections are detailed in Appendix A. Where appropriate, we have combined policy and claims summary information and financial information with information collected in our previous Northern Australia Insurance Inquiry. We note that policy level information is as at 30 September 2022 (before any insurer joined the pool), while policy and claims summary information and financial information was collected on a financial year basis. As such, while the periods overlap, there may be slight differences in values between figures.

There may also be differences between values provided as part of our first report and figures presented here. This is because we have collected additional historical data from a larger group of insurers, made further refinements to our methodology and updated our prices to 2022–23 dollars.

Further information on our data collection, methodology and refinements can be found in Appendix A. We will continue to build upon our data collection in future reports.

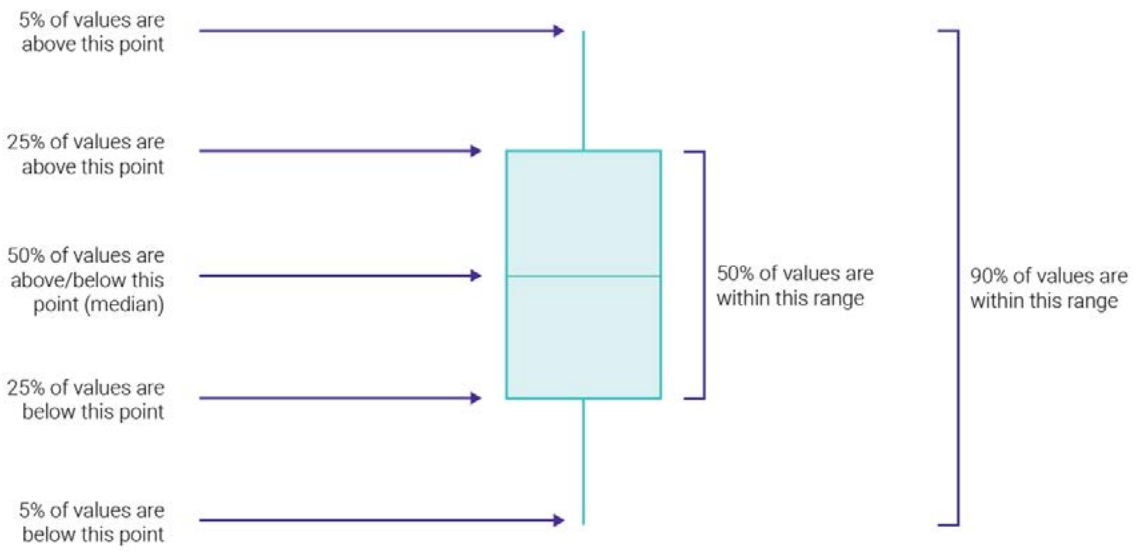
Our results are presented in the sections below. Noting the pool's impact is limited at this time and is still developing, we find that:

- insurance prices in northern Australia remain high, and increased sharply in 2022–23 in nominal terms
- policyholders in northern Australia have consistently paid more for their home and contents insurance compared to the rest of Australia. When accounting for differences in the sum insured, the gap is getting wider
- reinsurance remains a significant cost for insurers, and comprises a large portion of an average premium in northern Australia
- taxes, duties and levies have a considerably higher dollar impact on consumers in northern Australia as taxes are proportional to premiums.

7.1 Prices of home and contents insurance

This section provides analysis on home insurance prices – that is, the retail premiums that consumers pay insurers for their insurance policies. There are several factors that can affect the premium paid by a policyholder for insurance. In particular, 3 factors which can have a significant impact on the premium paid are the peril risk ratings that apply to the property, the amount for which the property is insured (sum insured), and the excess level selected. For this report, we look at insurance prices in several ways: average and the range of premiums (Section 7.1.1); premiums per $100,000 sum insured (Section 7.1.2); premiums by excess (Section 7.1.3); and premiums by sum insured and excess (Section 7.1.4).

In addition to providing average or mean values, we have included box plots showing the range of premium outcomes, where appropriate. The example below provides a guide on what these figures illustrate:



The box plots allow for a deeper look at the prices paid by a wider range of policyholders, including those in cyclone-prone regions in northern Australia. Due to some extreme values, the top and bottom 5% are not displayed in box plots to aid readability of the figures. As such, they may not necessarily reflect the individual experiences of particular policyholders and more recent changes in premiums. Where appropriate, we discuss the outcomes for the top 5% of policyholders. We will continue to closely watch broader pricing outcomes throughout our monitoring.

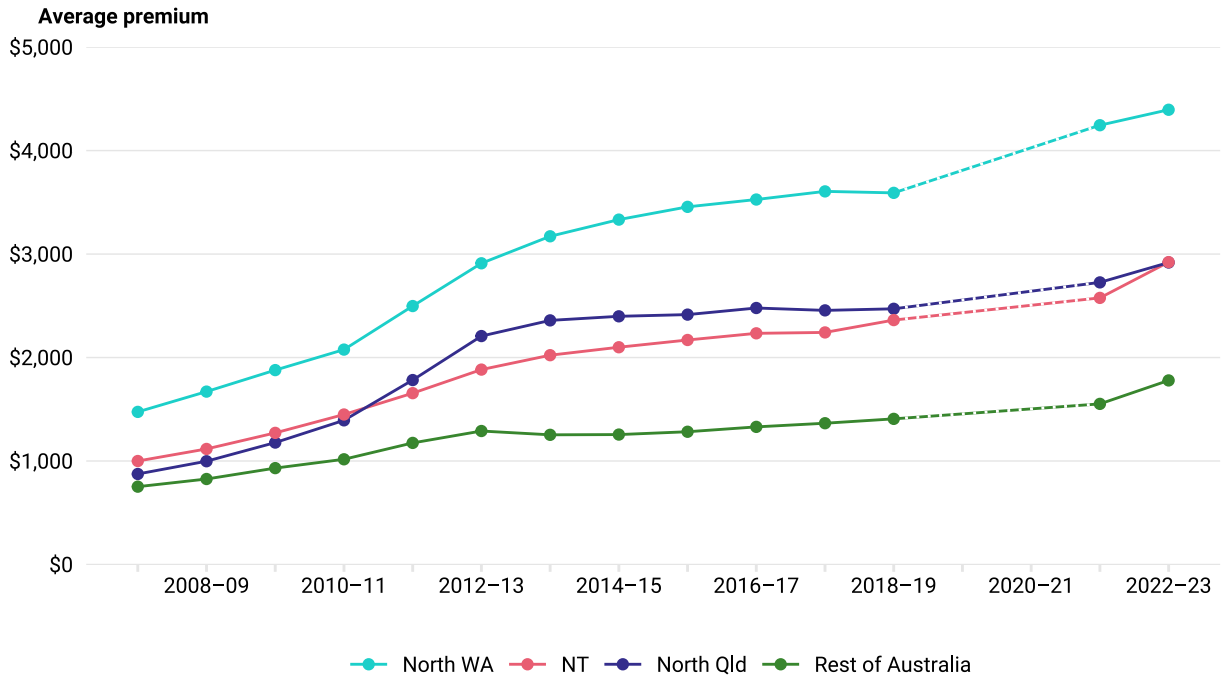
7.1.1 Premiums paid for home and contents insurance

This section analyses the premiums paid by policyholders for combined home and contents insurance. The average premiums presented are the mean value of the premiums for insurance products supplied by insurers at a postcode or regional level. They include GST, stamp duty and applicable levies. They represent actual prices paid by consumers for insurance products, including any commissions built into premiums, but do not include additional fees that may be applied by an insurance broker for arranging insurance. They do not include quoted premiums that were not ultimately taken up by consumers due to various reasons, including unaffordability.

Mean figures do not show the range of outcomes within regions. Where relevant, in this section we also present information on median results and show the range of premiums paid by policyholders for their combined home and contents insurance.

Figure 7.1 below shows that average premiums for combined home and contents insurance remained high in northern Australia and rose sharply in 2022–23 across all of Australia, in nominal terms. These nominal results may reflect the lived experience of policyholders when they compare the change in their premiums year on year. Average premiums in north Western Australia increased by 4% in nominal terms and remained the highest of the 4 regions at $4,395. The Northern Territory and north Queensland experienced increases of 13% (from $2,576 to $2,922) and 7% (from $2,726 to $2,918) respectively. The rest of Australia saw the largest percentage increase of 15% between 2021–22 and 2022–23 (from $1,552 to $1,779). The larger percentage increase for the rest of Australia may reflect the impact of significant disasters in southern parts of the country in 2022, although average premiums remained much higher in northern Australia.

Figure 7.1: Average premiums for combined home and contents insurance, by region, 2007–08 to 2022–23

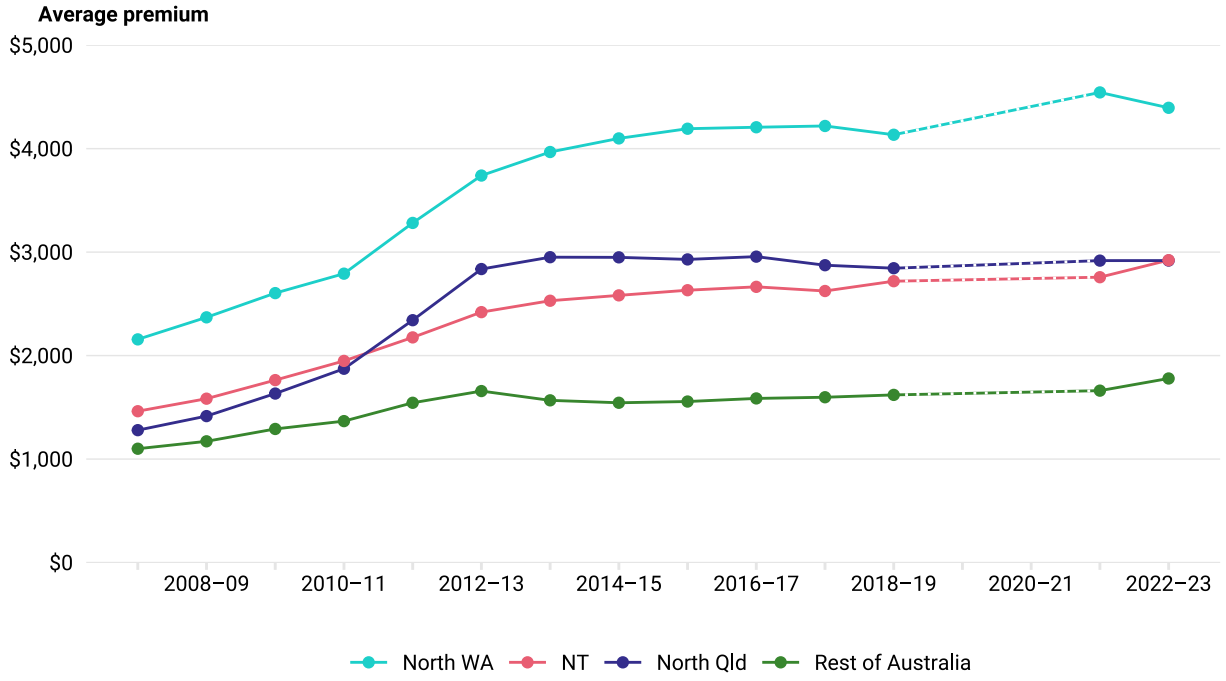


Source: ACCC analysis of data obtained from insurers.

As much of our price trend data is presented over a long period of time, the rest of this section presents figures in real terms (to 2022–23 dollars) where appropriate. This means that reported premiums for previous years have been adjusted to remove the effect of general price inflation on price trends.

Figure 7.2 below shows that average premiums for some regions increased between 2021–22 and 2022–23, in real terms. The Northern Territory experienced an increase in average premiums in real terms by 6% from $2,757 to $2,922. North Queensland stayed steady at around $2,918 year on year, while average premiums in north Western Australia decreased slightly by 3% (from $4,543 to $4,395), in real terms. The rest of Australia saw the largest increase of 7% in real terms, increasing from $1,661 to $1,779. As mentioned in relation to Figure 7.1 above, however, average premiums in northern Australia remained higher than the rest of Australia.

Figure 7.2: Average premiums for combined home and contents insurance, by region, 2007–08 to 2022–23, adjusted for inflation

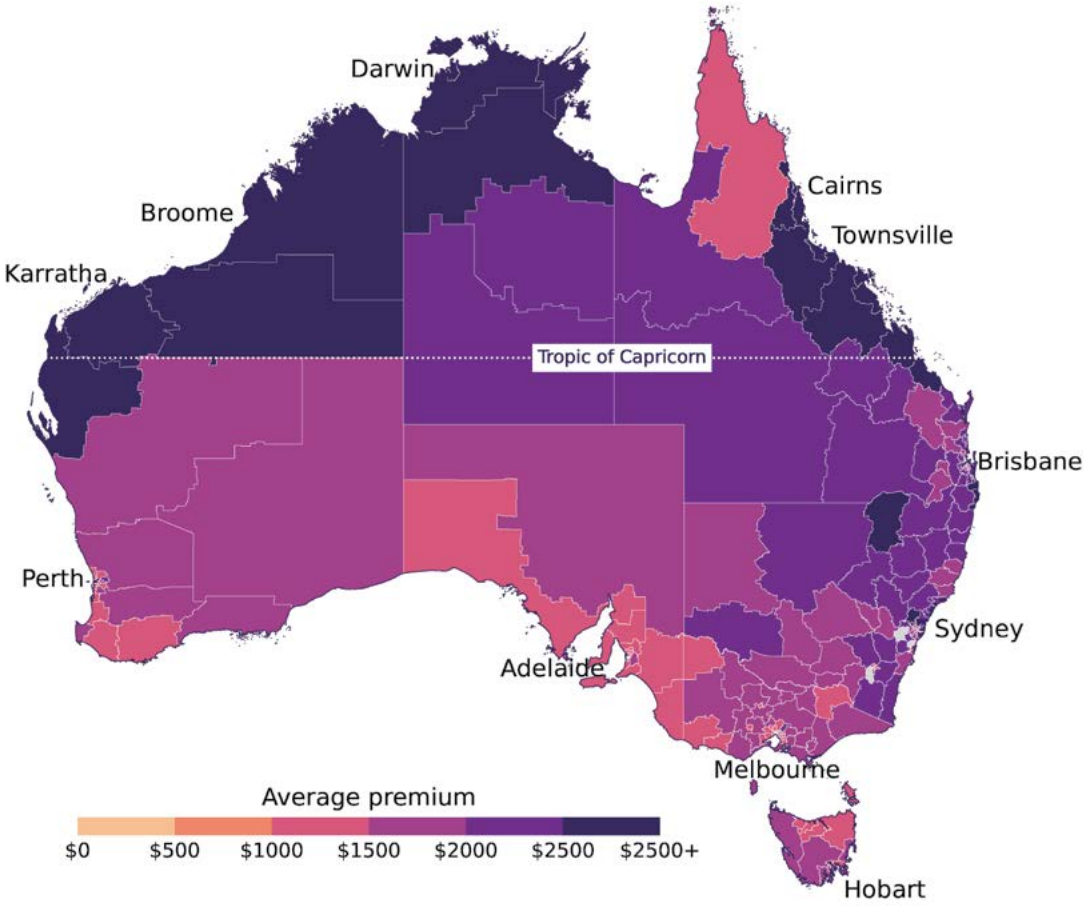


Source: ACCC analysis of data obtained from insurers.

Figure 7.3 below shows that average premiums for combined home and contents insurance in 2022 were highest throughout large areas of north Western Australia and some coastal areas of north Queensland. Average premiums were relatively high in the Northern Territory and generally lower outside of northern Australia. However, based on the data received, there were also pockets of high average premiums in areas of northern New South Wales, likely due to higher flood risk.[275]

275 The Institute of Actuaries of Australia, *Home Insurance Affordability Update*, August 2023, p 17.

Figure 7.3: Average premiums for combined home and contents insurance, by Statistical Area Level 3, 2022



Source: ACCC analysis of data obtained from insurers.

Average premiums for home and contents policies for properties at medium to high risk of cyclone in northern Australia were higher than in low cyclone risk areas.[276] For example, policies for properties at medium to high cyclone risk in north Western Australia had an average premium of $5,671. North Queensland had an average premium of $3,586, and the Northern Territory was $3,438. This compares to average premiums for properties with lower cyclone risk in north Western Australia ($2,038), north Queensland ($2,615) and the Northern Territory ($2,693).[277] Policies for properties at higher risk of cyclone are of particular interest because of the pool's objective to direct support and premium savings to households and small businesses in areas of medium to high cyclone risk (see Sections 1.2 and 5.1). These policies will be of particular focus over the course of our monitoring role.

Figure 7.4 below illustrates the spread of premiums paid by policyholders in 2022. To improve the readability of the chart, the top and bottom 5% are not displayed due to extreme values.[278]

The figure shows that, while combined home and contents insurance premiums were generally higher in all northern Australian regions compared to the rest of Australia, premiums in north Western Australia were both higher and more variable. Median premiums in north Western Australia ($4,016)

276 We considered policies in northern Australia with wind risk bands of between O and W (as defined by the ARPC) to be at medium to high risk of cyclone.

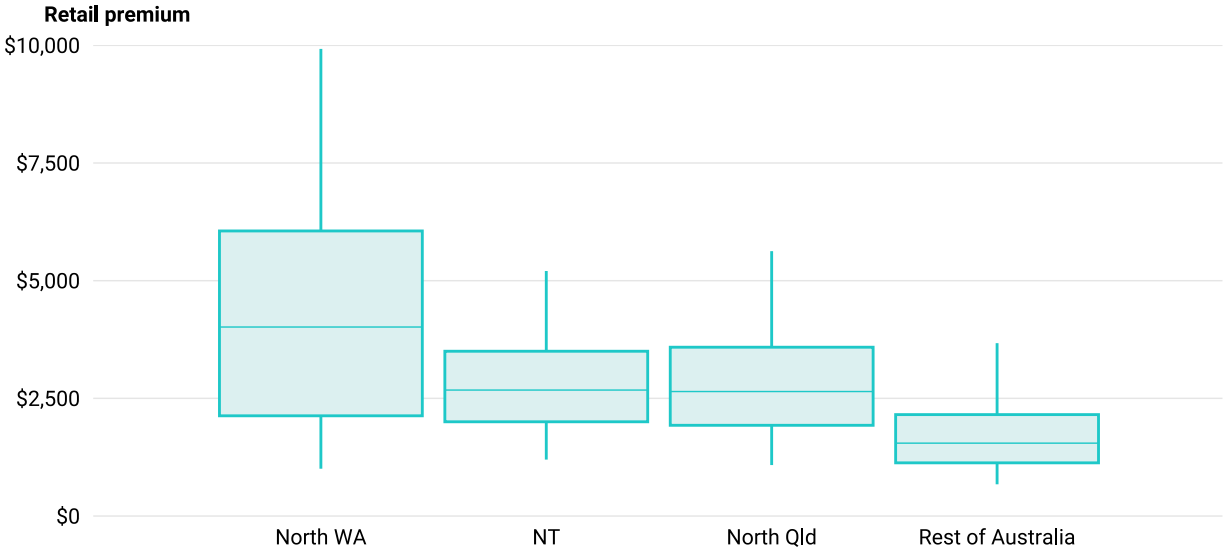
277 We used policy level information as at 30 September 2022 to produce these values. This is a different time period compared to Figures 7.1 and 7.2, which were produced using our policy and claims summary information collected on a financial year basis. While the periods overlap, there may be slight differences in values between figures.

278 We note that values not displayed in this figure are actual premiums faced by policyholders and are only removed for the purposes of clearly illustrating the experience of most policyholders. These values are included in calculations of the box plots, including the median. Further information on our methodology is provided in Appendix A.

were greater than the Northern Territory ($2,677) by 50%, north Queensland ($2,645) by 52%, and more than double the rest of Australia ($1,548). The top 5% of policyholders paid over $9,924 in north Western Australia, compared to $5,628, $5,206, and $3,673 respectively in north Queensland, the Northern Territory and the rest of Australia.

Of note, 88% of policyholders in northern Australia paid more than $1,500 for their premium, compared to 53% for the rest of Australia.

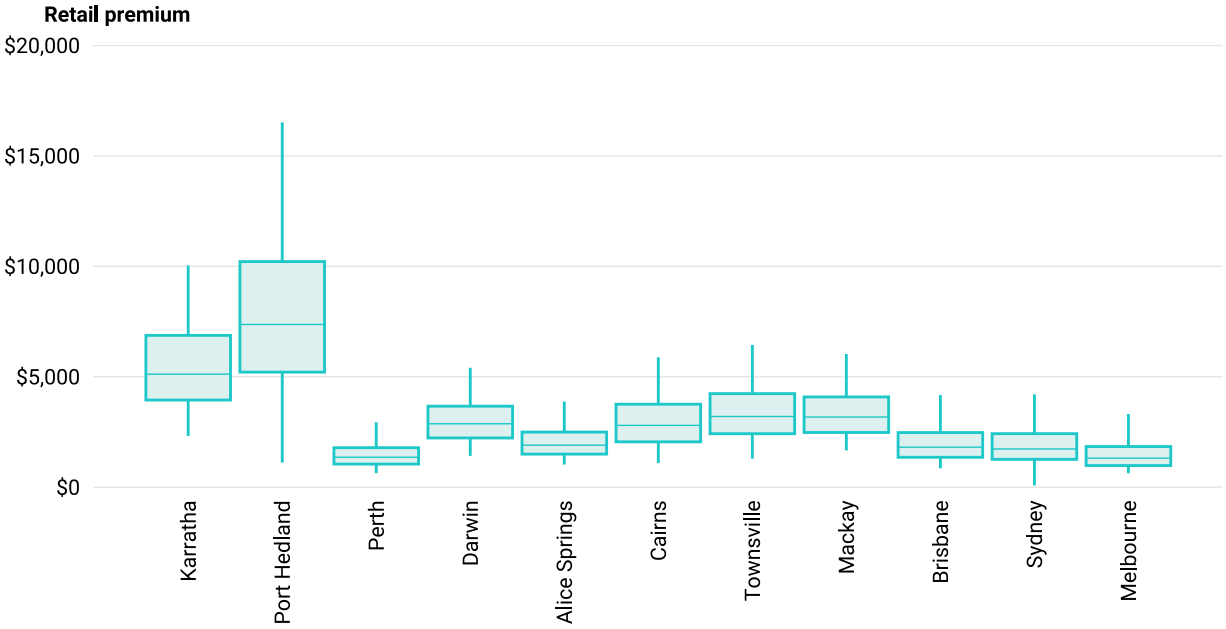
Figure 7.4: Distribution of retail premiums for combined home and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 7.5 below shows the distribution of combined home and contents premiums in select cities and towns. The highest median premiums were clearly faced by the northern cities of Port Hedland ($7,367), Karratha ($5,117), Townsville ($3,202), Mackay ($3,177) and Cairns ($2,799). The capital cities with the highest median premiums were Darwin ($2,871), Brisbane ($1,812) and Sydney ($1,731), while Melbourne and Perth had the lowest median prices of $1,316 and $1,356, respectively. Cities with the highest median premiums also tended to have the largest spread of premiums.

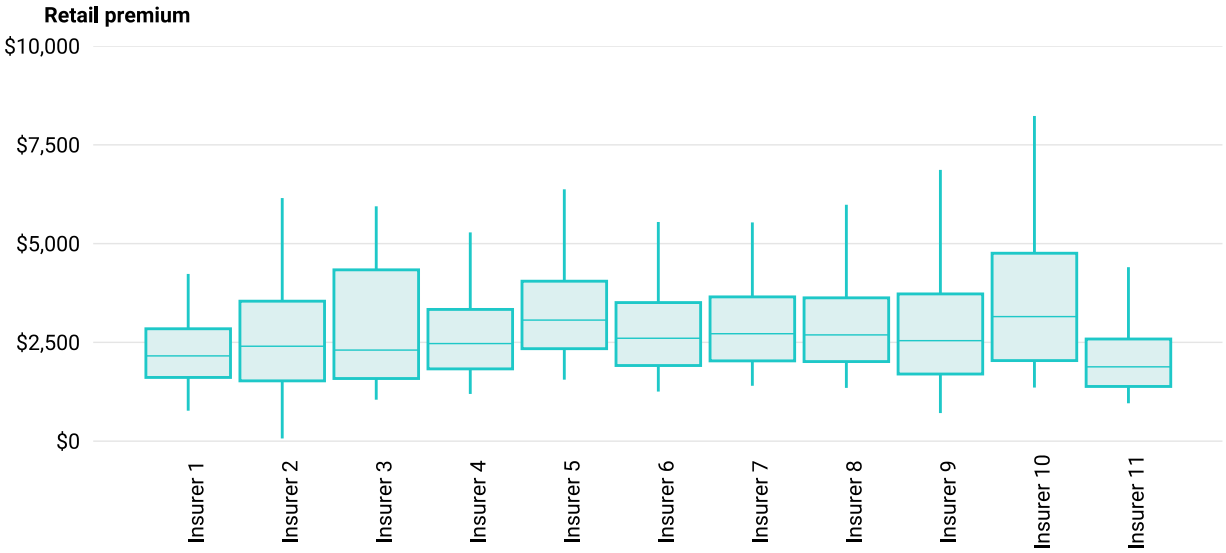
Figure 7.5: Distribution of retail premiums for combined home and contents insurance, select cities and towns, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 7.6 below shows the distribution of combined home and contents premiums in northern Australia by insurer. The median premium ranged from $1,881 (Insurer 11) to $3,153 (Insurer 10), with most insurers showing a wide spread of premiums. The differences in both the median and range of premiums between insurers could be due to different customer acquisition strategies or to a more selective customer retention strategy, rather than necessarily indicative of potential savings for all customers.[279] While the values presented are for northern Australia generally, insurers may choose to selectively target certain locations and/or types of risk within that region (availability of insurance is discussed further in Chapter 6).

Figure 7.6: Distribution of retail premiums for combined home and contents insurance by insurer, northern Australia, 2022



Source: ACCC analysis of data obtained from insurers.

279 ACCC, *NAII final report*, p 29.

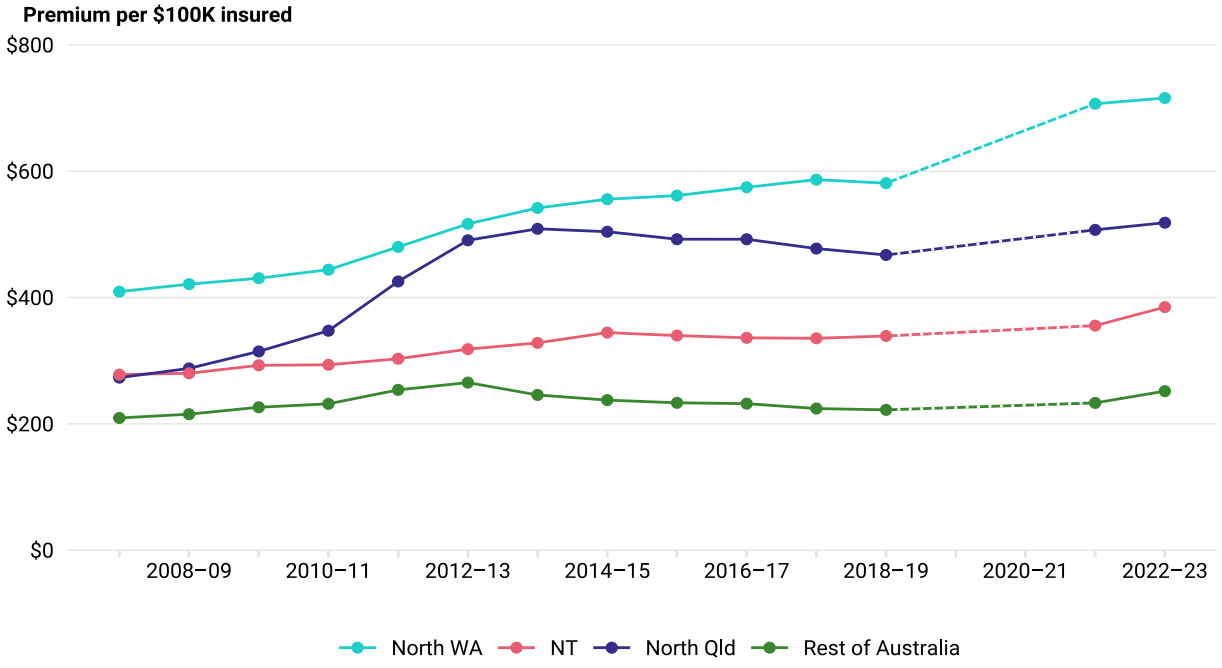
7.1.2 Premiums by sum insured

While the average premium figures presented above provide a good indication of the actual prices policyholders paid for insurance, they do not take into account the differences in the sums insured for different policies. The ACCC has previously found that sums insured have a large impact on premiums. While the exact effect will depend on a range of factors, the NAII final report found that increasing the building sum insured by $100,000 increases premium by between $200 and $400 in northern Australia.[280]

The estimated sum insured for a building will be based primarily on the estimated rebuilding cost (and in some cases, an extra allowance for ancillary costs). Building costs are generally higher in northern Australia for a variety of reasons, such as remoteness and the application of higher building standards.[281] As a result, a house with particular characteristics may have a considerably higher estimated sum insured in northern Australia than it would in a capital city.[282]

As shown in Figure 7.7 below, all regions experienced increases in average premiums per $100,000 sum insured in 2022–23, continuing the general trend since 2007–08. The Northern Territory experienced the joint largest increase, up 8% from the previous year, bringing the average premium per $100,000 sum insured to $385. The rest of Australia also experienced an increase of 8%, with an average premium per $100,000 sum insured of $252, although it remained the cheapest region. North Western Australia continued to have the highest average premium per $100,000 sum insured at $716, a 1% increase from the previous year. North Queensland remained second highest at $518, a 2% increase from 2021–22. As these increases are not of the same magnitude as the average premiums increases presented in Figure 7.2 (in nominal terms), it may be the case that the value of sum insured has also increased, but at a higher rate than premium increases. This may be a reflection of insurers offering higher sum insured to address the effects of inflation and rising construction costs (which are discussed in Chapter 2).

Figure 7.7: Average premiums per $100,000 sum insured for combined home and contents insurance, by region, 2007–08 to 2022–23



Source: ACCC analysis of data obtained from insurers.

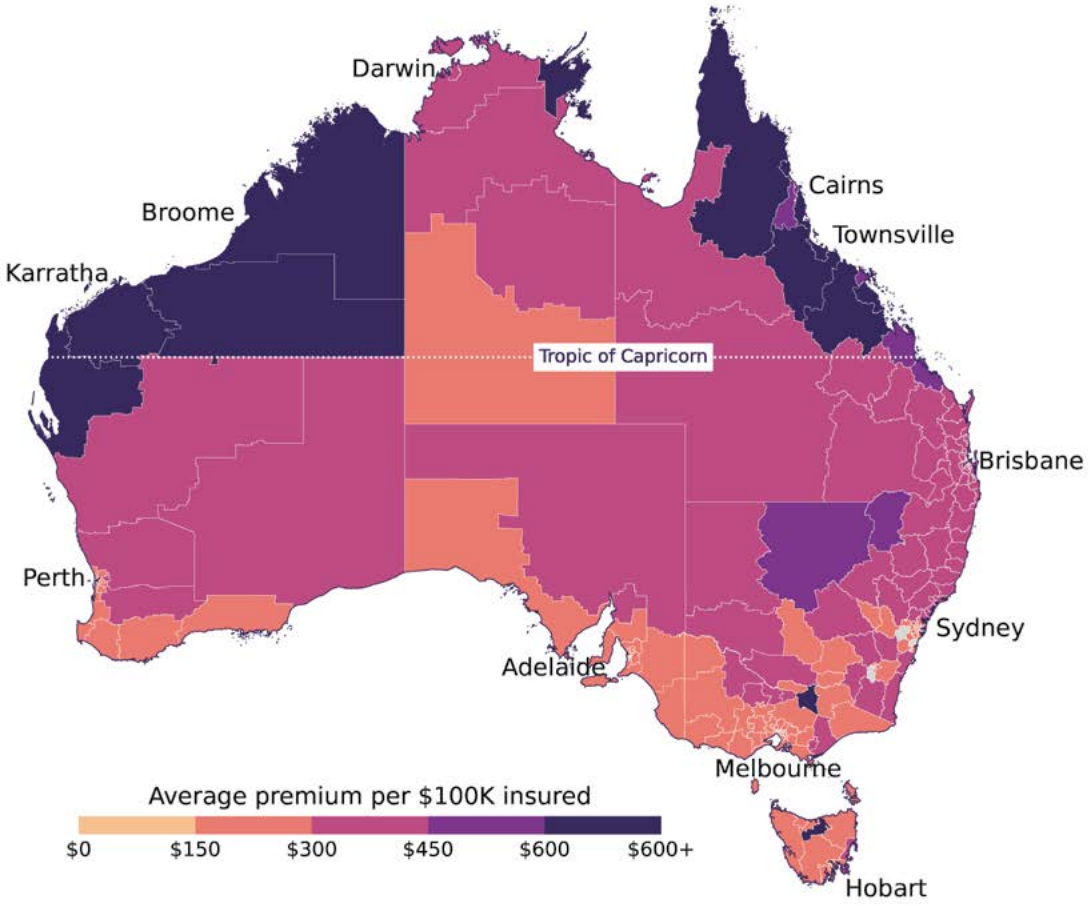
280 ACCC, *NAII final report*, p 32.

281 ACCC, *NAII final report*, p 32.

282 ACCC, *NAII final report*, p 32.

It is evident from the time series in Figure 7.7 that, irrespective of the year, consumers in northern parts of Australia have paid more for combined home and contents insurance even when the sum insured is factored into the average premium. Since 2013–14 many policyholders in northern Australia have consistently paid more than double for their combined home and contents insurance compared to the rest of Australia, even after accounting for differences in the sum insured, and the gap is getting wider. Additionally, this effect is more pronounced in northern coastal regions, as shown below in Figure 7.8.

Figure 7.8: Average premiums per $100,000 sum insured for combined home and contents insurance, by Statistical Area Level 3, 2022



Source: ACCC analysis of data obtained from insurers.

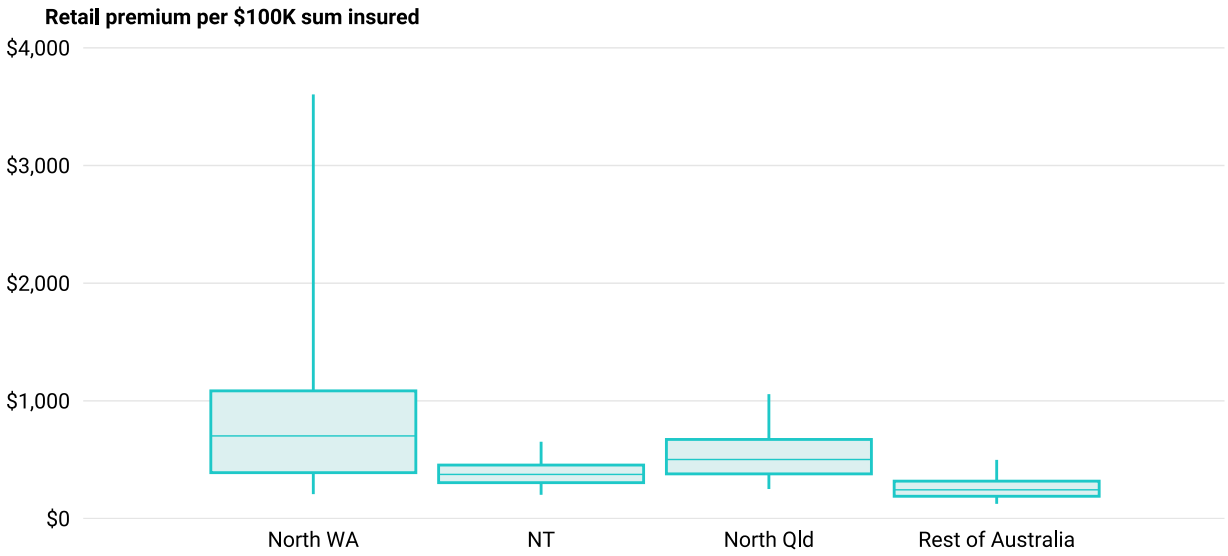
Figure 7.8 above shows the variability of average premiums per $100,000 sum insured for combined home and contents policies across Australia. The regions located above the Tropic of Capricorn generally paid higher premiums even when the sum insured was taken into account. North Western Australia consistently paid the highest premium per sum insured (more than $600). Certain locations in north Queensland, such as Townsville, also fell into the highest premium band paying more than $600 per $100,000 sum insured.

Figure 7.9 below shows that, even when accounting for the premium per $100,000 sum insured, the median combined home and contents premium for both north Western Australia ($702) and north Queensland ($502) was well above the levels observed for the Northern Territory ($375) and the rest of Australia ($244). North Western Australia had the highest median and also the largest spread in prices.

For the northern regions, 90% of policyholders had higher prices per sum insured than the average for the rest of Australia. For north Western Australia, north Queensland and the Northern Territory

at least 77% of policies had premiums per $100,000 sum insured above $300. In comparison, only 30% of policies were above $300 for the rest of Australia.

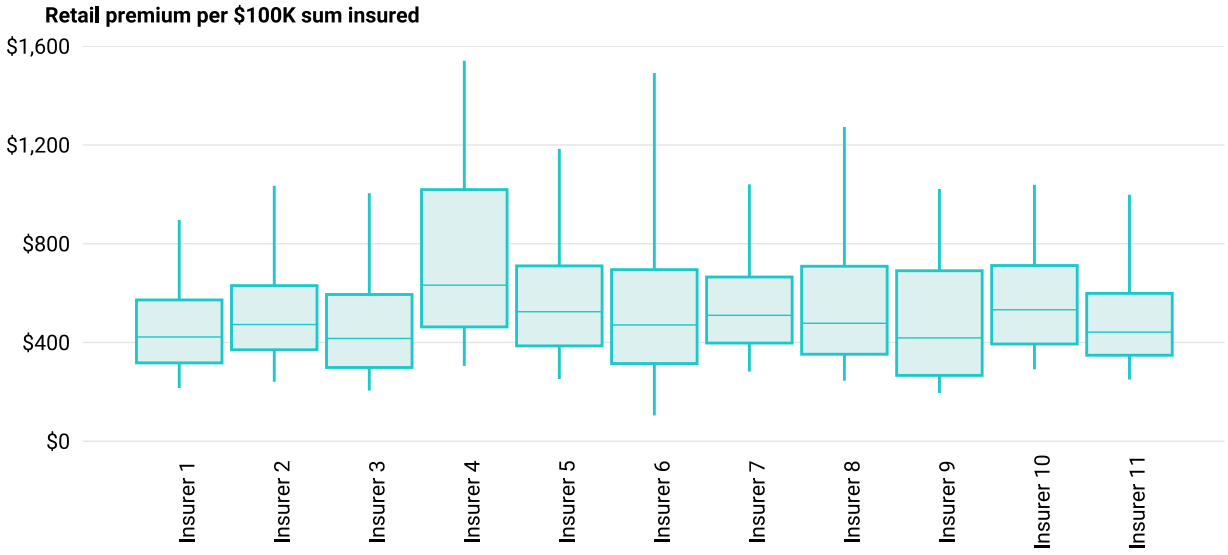
Figure 7.9: Distribution of retail premiums per $100,000 sum insured for combined home and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 7.10 below shows that there was high variability in the premiums per $100,000 sum insured charged by insurers for combined home and contents policies in northern Australia. Insurer 4 recorded the highest median ($632) of all insurers, and Insurer 6 displayed the greatest spread of prices per sum insured, while Insurer 3 had the lowest median ($416). Apart from Insurer 4, most other insurers were somewhat comparable to each other, with median premiums per $100,000 sum insured between $400 and $550. As with Figure 7.6, the differences in both the median and range of premiums between insurers could be due to insurers selectively targeting certain locations and/or types of risk within that region (as discussed in Chapter 6).

Figure 7.10: Distribution of retail premiums per $100,000 sum insured for combined home and contents insurance, select insurers, northern Australia, 2022



Source: ACCC analysis of data obtained from insurers.

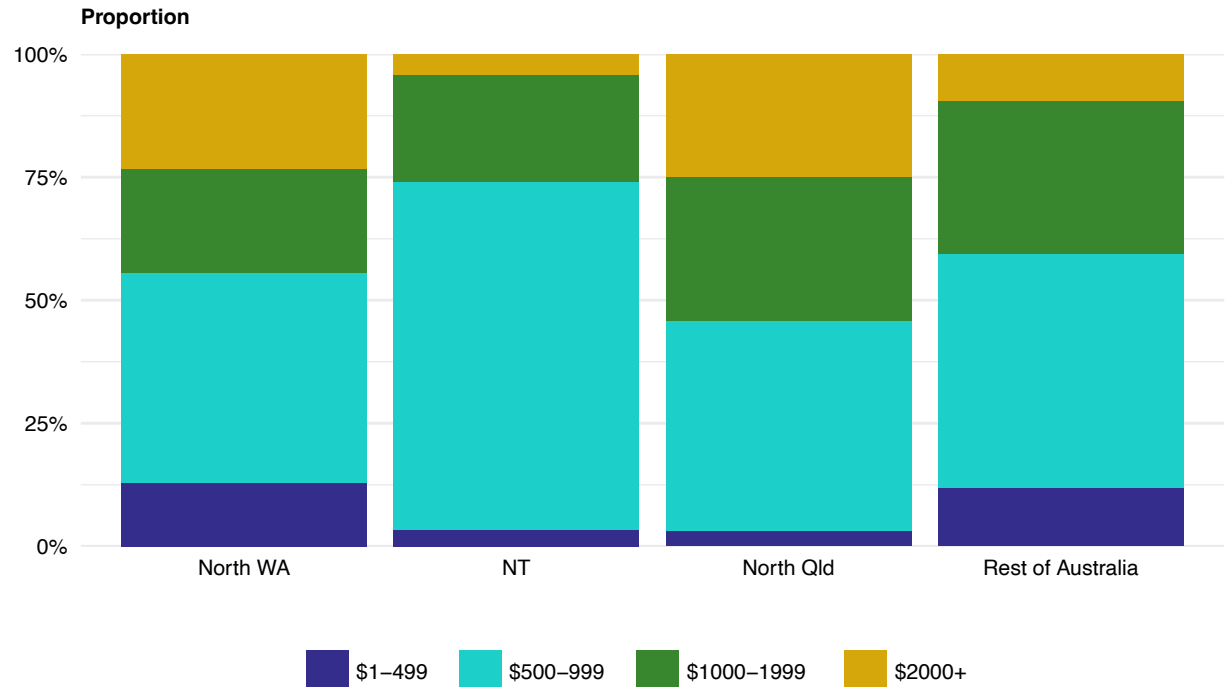
7.1.3 Premiums by excess

This section presents our analysis on the excess levels selected by policyholders, and average premiums when excess is accounted for. An insurance excess is the amount of money a policyholder is required to pay towards the costs of a claim they make, and is one of the limited options open to the policyholder to adjust the premium rate of their policy. The higher the excess a policyholder selects, the lower their premium will be, but equally the overall value of the policy is lower as it is less economical to make a small claim. Therefore, it is important to consider the excess levels when interpreting premium levels and movements.[283] Historically the trade-off between excess and premiums has meant higher excess levels in northern Australia as consumers try to reduce their high and rising premiums.[284]

Figure 7.11 below shows the proportion of combined home and contents policies in each excess band by northern Australian regions in 2022. Excess levels in north Queensland and north Western Australia were on average higher than in the rest of Australia. One quarter (25%) of north Queensland policies and 23% of north Western Australia policies had an excess of over $2,000, compared to only 9% in the rest of Australia. In comparison, the Northern Territory only had 4% of policies with an excess of above $2,000 and 22% with an excess between $1,000 and $2,000. The rest of Australia had 31% between $1,000 and $2,000.

As shown in Figures 7.1 and 7.2 above, north Western Australia and north Queensland paid higher premiums than the other regions. A possible explanation for these observations is that policyholders from more expensive regions may be choosing higher excesses to keep premiums lower than they would otherwise be with smaller excesses.

Figure 7.11: Proportions of excess brackets for combined home and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

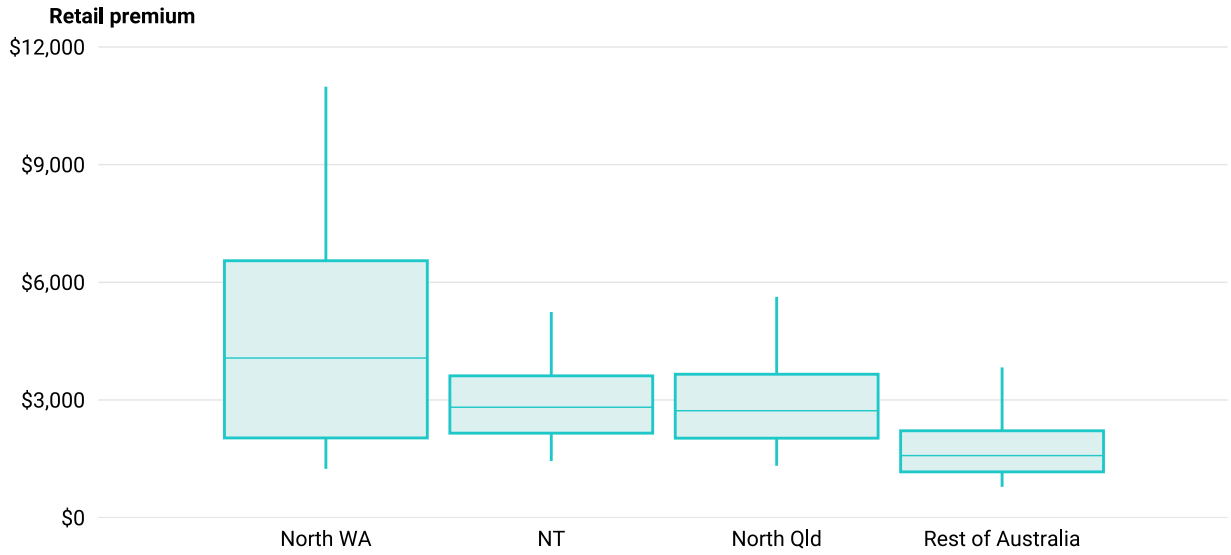
Figure 7.12 below shows the premium distribution for combined home and contents across northern regions for policies with 'typical' excesses between $500 to $1,000. North Western Australia had the largest spread, with 90% of prices ranging from $1,245 to $10,988, and also the highest median

283 ACCC, *NAII final report*, p 41.

284 ACCC, *NAII final report*, p 43.

of $4,069. North Queensland ($2,726) and the Northern Territory ($2,815) also had higher medians than the rest of Australia ($1,582). The chart illustrates that, even when considering only policies with similar excess amounts, northern Australian regions continue to pay more than the rest of Australia.

Figure 7.12: Distribution of retail premium for combined home and contents insurance, excess between $500 and $1,000, by region, 2022



Source: ACCC analysis of data obtained from insurers.

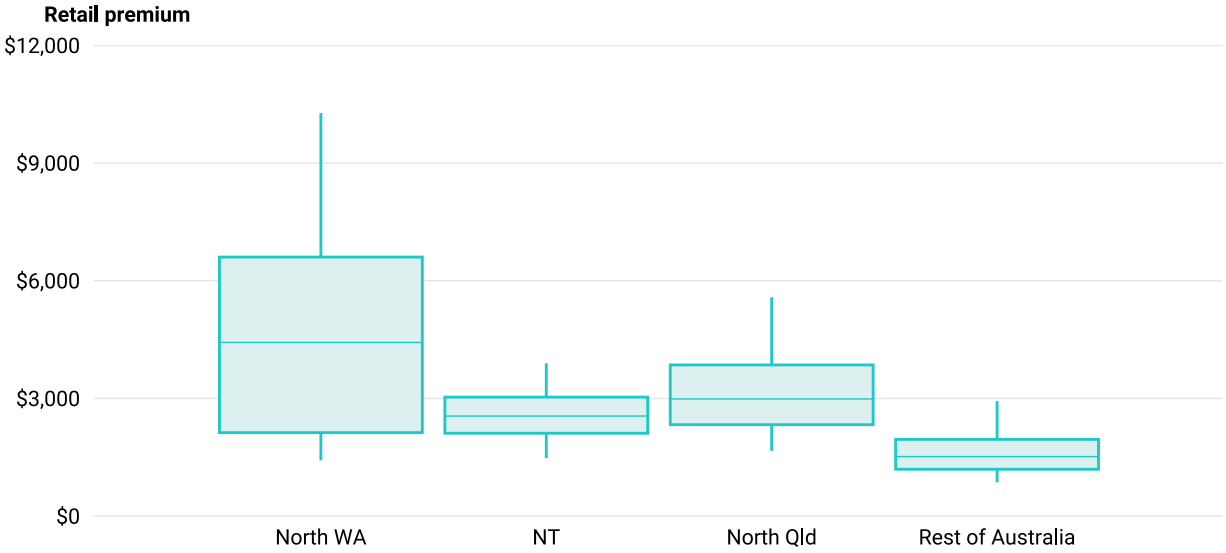
7.1.4 Premiums by excess and sum insured

In this section, we present analysis on the average premiums paid by combined home and contents policyholders within select sum insured and excess levels, and see the extent of any differences in outcomes when both these variables are controlled for.

We compare average premium outcomes by insurer and between regions when 'typical' sum insured and excess levels are selected. It should be noted that the sum insured and excess bands selected are based on a typical range of values for combined home and contents policies. However, they may not be the typical or most common sum insured or excess level for a particular insurer or a particular region.

Figure 7.13 below shows the premium distribution for combined home and contents across regions for 'typical' combined home and contents policies with excesses between $500 to $1000 and sum insured values of $500,000 to $800,000. Similar to findings in Section 7.1.1, we find that even holding excess levels and sum insured values to a 'typical' level, average premiums were still higher in northern Australia. The median retail premium was highest in north Western Australia at $4,427, followed by north Queensland ($2,987), the Northern Territory ($2,552) and then the rest of Australia ($1,518). The spread was also greatest for the regions with the highest retail premiums, particularly in north Western Australia.

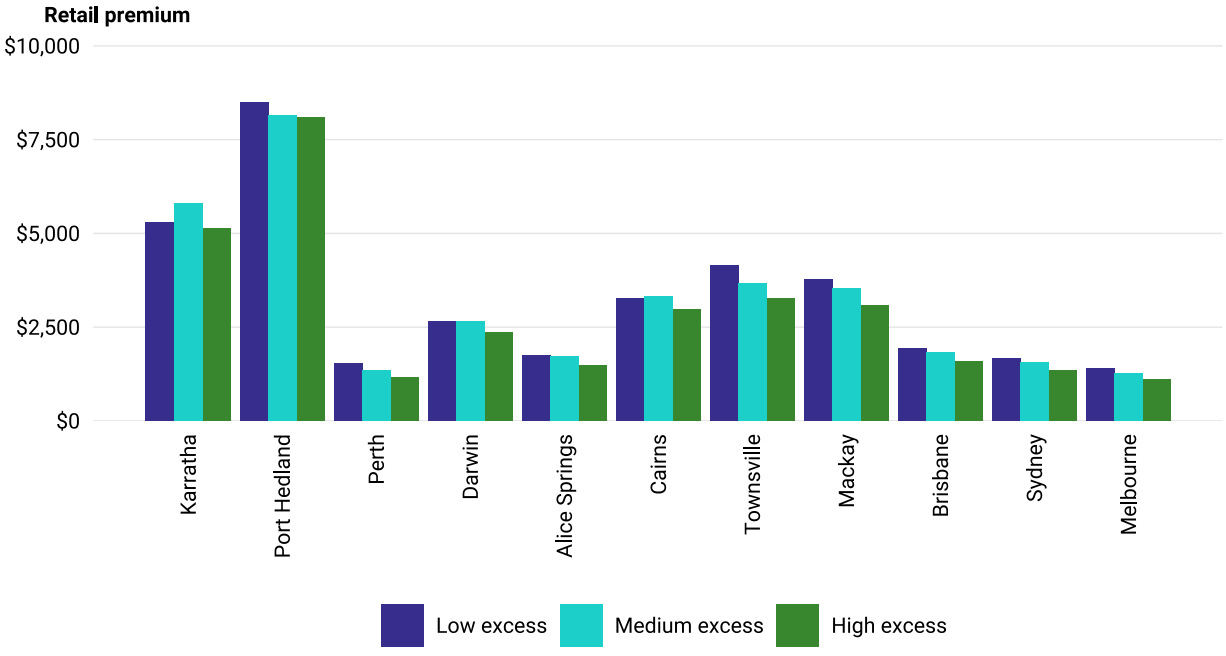
Figure 7.13: Distribution of retail premiums for combined home and contents insurance, excess between $500 and $1,000, sum insured between $500,000 and $800,000, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 7.14 below shows median premiums for combined home and contents across select cities and towns for sum insured values of $500,000 to $800,000, by excess bands. The following excess bands were selected: $0 to $499 for low, $500 to $1,000 for medium, and more than $1000 for high. The figure shows that, for most case study locations, policyholders who paid higher excesses paid lower premiums compared to other policyholders in the same region. The difference between the premiums for high and low excess bands was most clearly seen for locations that were paying higher premiums, such as Mackay and Townsville. Thus, the relationship between higher excesses and lower premiums per sum insured in Figure 7.14 seems to support the possibility that consumers may have selected higher excesses in order to limit a rise in their premiums.

Figure 7.14: Median premiums by excess bands for combined home and contents, sum insured between $500,000 and $800,000, select cities and towns, 2022



Source: ACCC analysis of data obtained from insurers.

7.2 Breakdown of insurance premiums

This section provides a breakdown of retail premiums and examines insurer costs for combined home and contents insurance products in different regions across Australia. The breakdown of retail premiums for all home and contents insurance products in northern Australia are examined in Section 7.2.1, while insurer costs are examined in Section 7.2.2.

7.2.1 Breakdown of retail premiums

While each insurer's exact approach will differ, generally retail premiums are built up using a broadly similar approach across insurers. As detailed in Section 4.2 insurers first calculate a technical premium, which reflects the insurer's estimate of the cost of providing insurance with a margin added for profit or return on capital.

Once the technical premium is calculated, insurers often make premium adjustments, which can increase or decrease the consumer's charge compared to the technical premium. Adjustments can be made by insurers for a range of reasons, such as competitive or market positioning, or to manage their exposure. Discounts may also be applied for reasons such as an online purchase, no claims bonus, or multi-policy discounts.

The final step is applying surcharges, taxes, duties, and levies to arrive at the retail premium, which will increase the amount paid by the end consumer. Surcharges can be included for things such as monthly payment options. The insurer will then add any relevant levies, taxes, and duties to give the final 'retail premium'.[285]

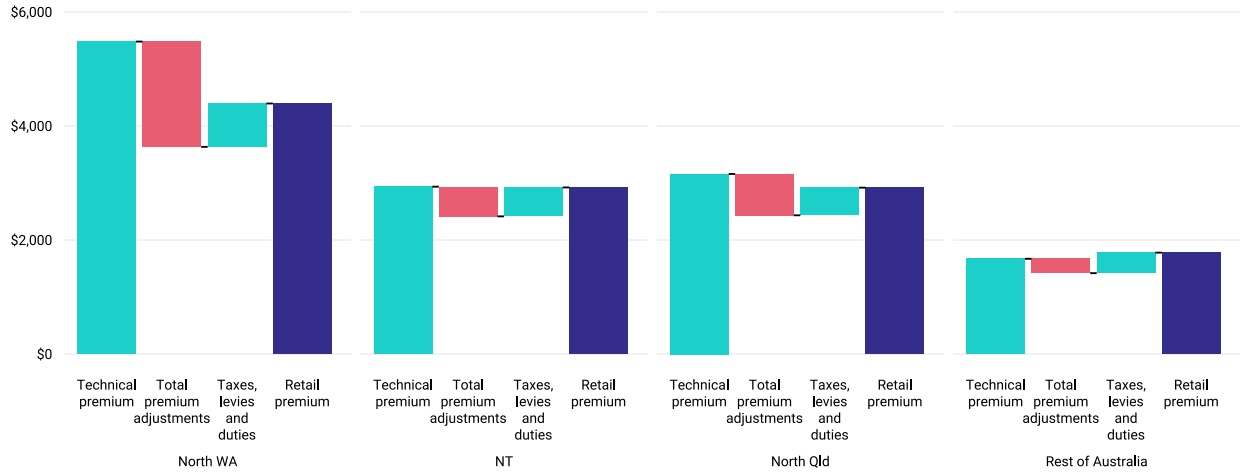
We provide more detailed explanation on how insurers 'build' premiums in Chapter 4.

Figure 7.15 below shows the average result of each of these steps to calculating the retail premium for combined home and contents insurance products in northern Australian regions as at September 2022. We note that only records with complete (in other words, not missing any of) technical premium, premium adjustments, taxes and levies, and retail premium values were included in the below analysis. This means that the figures represent a large, but not complete, proportion of policies from the data we obtained.[286]

285 ACCC, *NAII final report*, p 61.

286 The proportion of policies with complete data by region is as follows: north Queensland (62.2%), north Western Australia (55.2%), Northern Territory (22.9%), and rest of Australia (75.5%).

Figure 7.15: Average retail premium breakdown for combined home and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.
Note: Only complete records containing technical premium, premium adjustments, taxes and levies and retail premium values have been included in this analysis.

Consistent with our findings in Section 7.1, north Western Australia had the highest average technical premium at $5,480, followed by north Queensland at $3,158 and then the Northern Territory at $2,936. The rest of Australia had the lowest average technical premium of $1,671. As explored further in Figure 7.16 below, higher average technical premiums in northern regions, particularly north Western Australia and north Queensland, are reflective of the higher expected claims costs in those areas. This is likely due to the higher natural peril risks in northern Australia, particularly for flood and cyclone.[287]

Technical premiums reduced on average across all regions due to premium adjustments and discounts applied by insurers. Regions with the highest technical premiums experienced the greatest premium adjustment reductions. North Western Australia had the largest premium adjustment decrease, on average a reduction of $1,846, followed by north Queensland with $724, the Northern Territory with $520, and then the rest of Australia with $252.

As explained in Section 4.3, insurers apply adjustments for a variety of reasons, including concentration risk, market adjustments, price optimisation, and capping or cupping. To some degree, these negative adjustments may be indicative of 'capping', which is where insurers limit price increases in any given year in order to minimise price shock for consumers at renewal. However, adjustments are usually temporary and these price increases to the technical premium will likely flow through to the retail premium at subsequent renewals. Trends which are placing upward pressure on the price of insurance, such as inflation and increased reinsurance costs, are discussed in detail in Section 2.3.

Taxes and duties applying to general insurance include GST and state and territory stamp duties and (in some jurisdictions) other levies. These are not a cost to the insurer, who passes them through in the final bill, but they are an added cost incurred by the customer. Both GST and duties are proportional to the premium, so the amount paid is higher in areas where technical premiums are higher. For example, north Western Australia had the highest average technical premium, and the highest average taxes and duties of $760. The rest of Australia had the lowest average taxes and duties of $360 due to having the lowest average technical premium.

Table 7.1 below shows tax rates applied for home, contents, strata and SME insurance by state and territory. As stamp duties are applied on the GST inclusive amount of a premium, the effect of these

287 ACCC, *NAII final report*, p 45.

duties is magnified. The taxes imposed on home, contents, strata, and SME insurance mean that premiums charged by insurers are magnified by 19.9% in Queensland and by 21% in the Northern Territory and Western Australia. As premiums grow in northern Australia, so too does the dollar value of the amount paid in GST and stamp duty (which is levied on the GST-inclusive premium amount).[288]

Table 7.1: Tax rates applied for all home, contents, strata, and SME insurance, by state and territory

	NSW and QLD	NT, VIC, TAS and WA	SA	ACT
Stamp Duty	9%	10%	11%	-
GST	10%	10%	10%	10%
Combined tax rate	19.9%	21.0%	22.1%	10.0%
Tax as a proportion of the retail premium	16.6%	17.4%	18.1%	9.1%

Source: State and territory governments' websites.

Additionally, New South Wales currently imposes an emergency services levy on insurance policies.[289] The exact amount for the New South Wales emergency services levy varies each year but added around 18% to all home and contents insurance premiums, and up to 40% to business cover in 2022–23.[290] Tasmania also currently imposes an insurance fire levy of 28% on premium income for certain prescribed classes of business insurance.[291]

After taking into consideration adjustments to the technical premiums, we find that north Western Australia had the highest average retail premium of $4,395, followed by the Northern Territory with $2,922, north Queensland with $2,918 and then the rest of Australia with $1,779. Each of these retail premiums for northern Australian regions were less than the technical premium. This suggests insurers may not be charging enough to cover the estimated cost of providing insurance in these regions. Over the longer term, this trend may indicate further price increases, which may offset any savings from the pool. The profitability of providing insurance in northern Australia is considered further in Section 10.3.

7.2.2 Insurer costs incurred

This section provides information on the costs incurred by insurers supplying all home and contents insurance products. These costs can be divided into the following categories:

- Claims costs – This includes costs such as the claims incurred and the cost of handling and assessing claims. These costs tend to vary with the number of policies written and the relative risk to the property insured. In this section we use a 'net claims expense' measure of claims costs. Net claims expense is a measure of how expensive the claims were for the insurer, accounting for reinsurance and non-reinsurance recoveries.
- Reinsurance costs – This includes the cost of premiums paid to reinsurers. These costs tend to vary with the type of reinsurance purchased, the number of policies written, the sum insured under the policies written, and the relative risk of the properties insured. Once insurers join the pool, the effect on insurers costs should be most directly felt in this cost category, which will

288 ACCC, *NAII final report*, p 54.

289 The New South Wales Government has announced plans to reform the emergency services levy: InsuranceNews.com.au, *NSW to ditch current insurance-funded Emergency Services Levy*, 16 November 2023, InsuranceNews website, accessed 17 November 2023.

290 ICA, *'Find a fairer way' to fund NSW emergency services* [media release], ICA, 13 February 2023, accessed 28 September 2023.

291 The Tasmanian Government is currently reviewing the funding model for the Tasmania Fire and Emergency Service. Felix Ellis, Minister for Police, Fire and Emergency Management, *Securing the future of our Fire and Emergency Services*, [media release], 28 September 2023.

include both the reinsurance premium paid to ARPC and the reinsurance premiums paid to other reinsurers for risks not covered by the pool.

- Underwriting costs – This includes levies, charges, and acquisition costs which are incurred in obtaining and recording insurance contracts. These costs include selling and underwriting costs such as advertising and risk assessment, the administrative costs of recording policy information and premium collection costs. We have excluded commission costs from this category and have reported on this separately (see below).
- Commission costs – This includes the costs of commission or brokerage paid to an intermediary for obtaining business for the insurer.[292]

Government cost categories which also apply to consumers, such as GST, stamp duty, and other government charges, are not considered here.

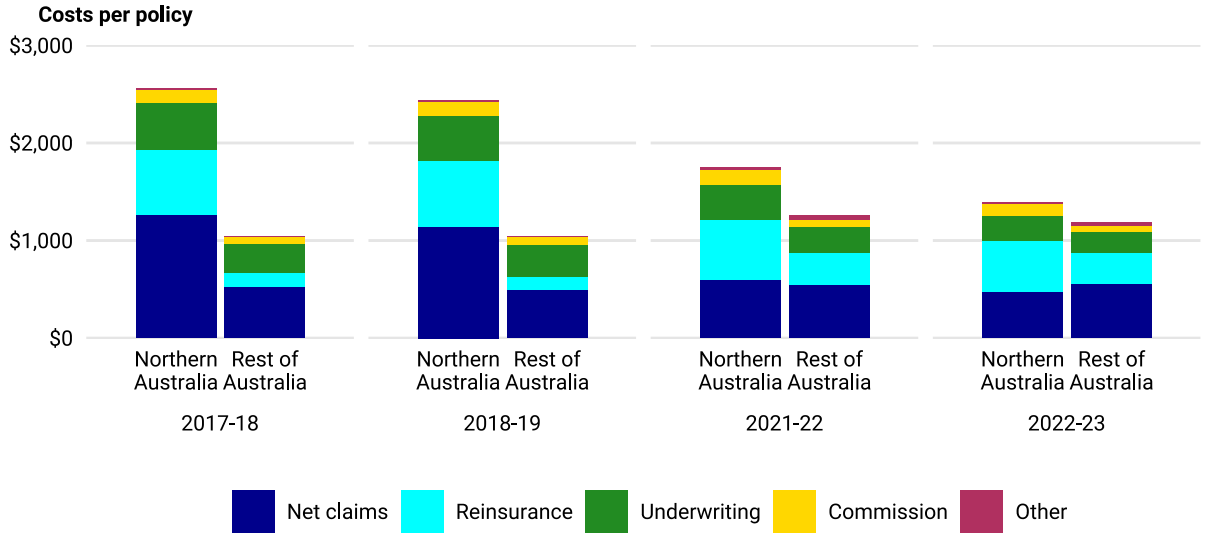
It should be noted that costs incurred are not directly used to calculate premiums. Instead, insurers use modelling to forecast costs they anticipate they will likely incur over the duration of the policy. As actual costs will not always align with forecasted costs, this can result in insurers over or under collecting sufficient premium to cover their expenses in any given year.

Figure 7.16 compares the average cost by cost category for all home and contents policies for 2017–18, 2018–19, 2021–22, and 2022–23, for northern Australia compared to the rest of Australia. Over this period, the average cost per policy has been rising in the rest of Australia in real terms (from $1,047 in 2017–18) before steadying in the last year at $1,190. This is being driven by increases in reinsurance cost per policy from $142 in 2017–18 to $317 in 2022–23. Commission costs have been steady in the rest of Australia and underwriting costs have decreased over this time in both northern Australia and the rest of Australia.

Average costs incurred per policy in northern Australia have decreased in real terms from $2,563 in 2017–18 to $1,399 in 2022–23. Reinsurance and commission costs decreased slightly. The overall decrease is largely due to a substantive decrease in average net claims cost (from $1,255 in 2017–18 to $464 in in 2022–23) to levels below that of the rest of Australia ($553 in 2022–23). This is likely due to the low number of significant events impacting northern Australia over the past 2 years compared to the rest of Australia.

292 ACCC, *Insurance monitoring*, p 43.

Figure 7.16: Average cost incurred per policy by cost categories, all home and contents insurance, by region, 2017–18 to 2022–23, adjusted for inflation



Source: ACCC analysis of data obtained from insurers.

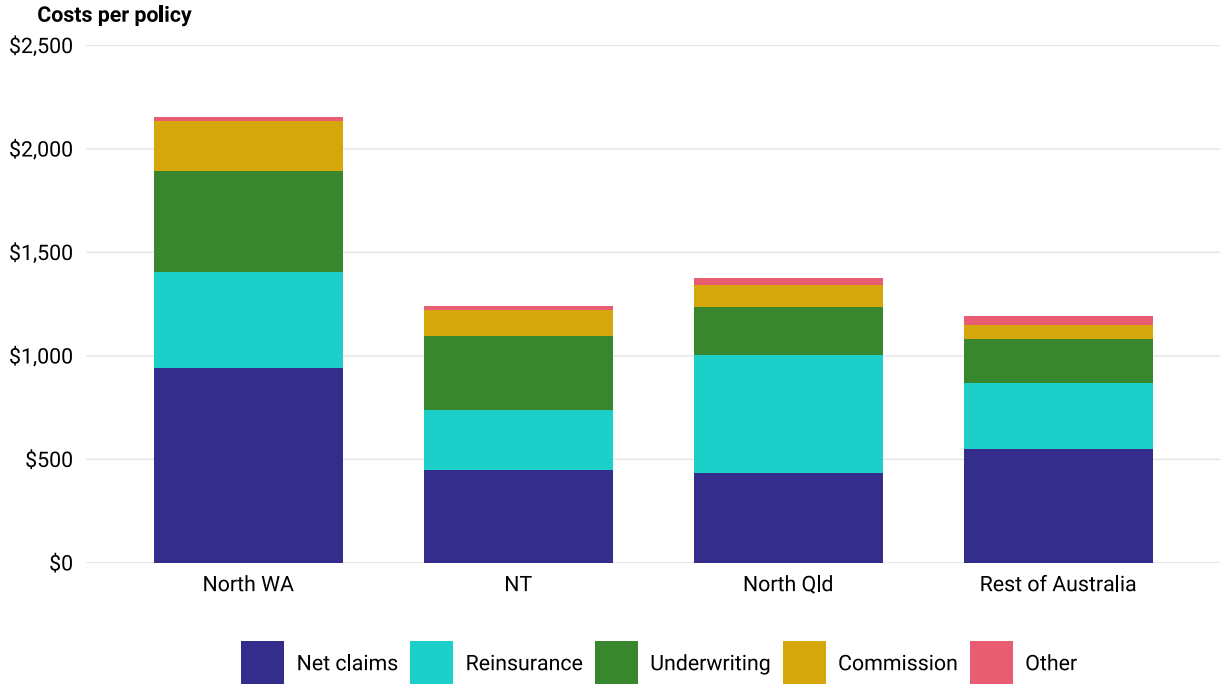
Figure 7.17 below shows the average allocation of costs incurred per home and contents policy across northern Australia and the rest of Australia in 2022–23. Consistent with its higher average premiums, north Western Australia had the highest average net claims costs per policy compared to the other regions at $940, and all the above defined cost categories except for reinsurance where it was second ($467). North Queensland had the lowest net claims at $435, but had the highest reinsurance costs at $569. The rest of Australia had the second highest net claims cost at $553, but the second lowest reinsurance cost at $317. This is indicative of the higher levels of reinsurance insurers purchase to cover northern Australian policies compared to the rest of Australia. This is not the case for the Northern Territory though, where reinsurance cost is similar to the rest of Australia at $293.

Commission costs incurred were the highest in north Western Australia at $241 per policy, and the lowest in the rest of Australia at $71 per policy. The Northern Territory and north Queensland have the second and third highest commissions at $130 and $105 respectively. This is driven by the proportional nature of commissions where higher average premiums will result in higher average commissions, but could also indicate a higher usage of brokers in northern Australia.

Underwriting costs were the highest in north Western Australia and the Northern Territory at $485 and $355 per policy, respectively, and the lowest in north Queensland and the rest of Australia at $233 and $211. This is likely related to the remote nature of several communities in north Western Australia and the Northern Territory compared to the more urbanised centres in north Queensland, and particularly across the rest of Australia.

Overall, in 2022–23 policies in north Western Australia had the highest average cost per policy at $2,152, and the rest of Australia had the lowest, with $1,190. North Queensland and the Northern Territory were similar to the rest of Australia at $1,375 and $1,242, respectively. These 3 regions having similar average costs is not always the case historically and is something we will continue to monitor in future reports.

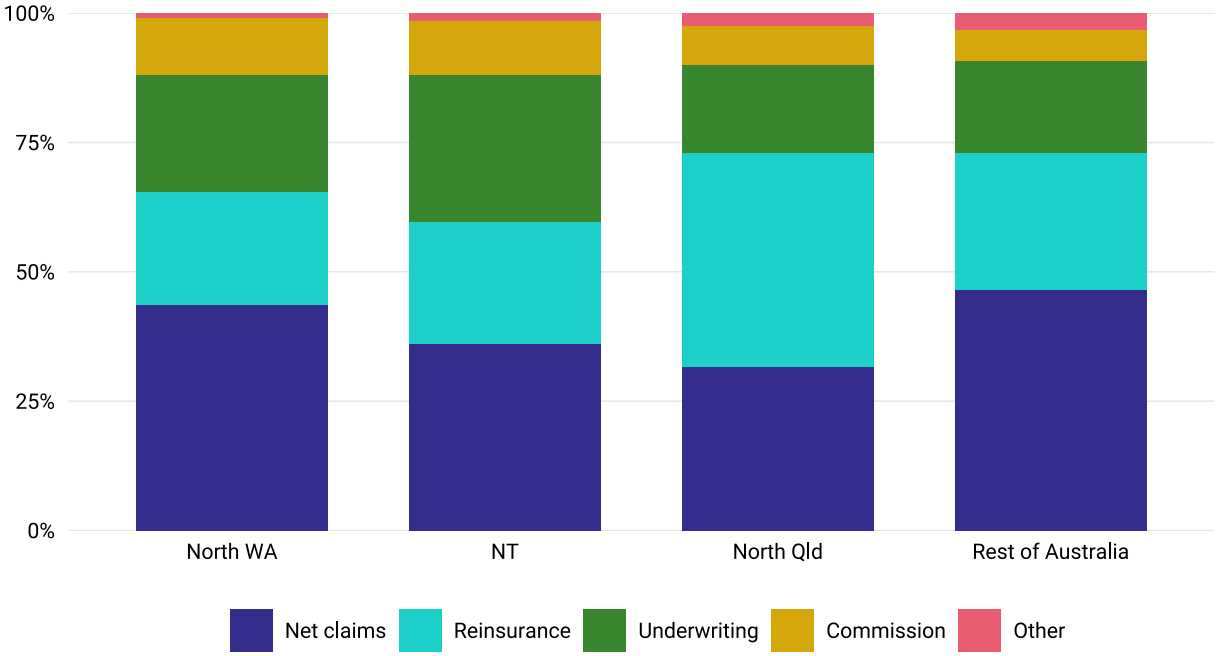
Figure 7.17: Average cost incurred per policy by cost categories, all home and contents insurance, by region, 2022–23



Source: ACCC analysis of data obtained from insurers.

Figure 7.18 shows the proportion of cost categories for all home and contents insurance policies across northern Australia and the rest of Australia in 2022–23. Net claims and reinsurance cost make up at least 65% of the cost per policy in all regions except the Northern Territory, where they make up 60%. The net claims cost makes up the largest proportion of cost for the rest of Australia, at 46%. Reinsurance expense was the highest in north Queensland at 41%, with the other 3 regions all between 22% and 27%. The proportion of underwriting costs were the highest in the Northern Territory and north Western Australia at 29% and 23%, respectively. Commission costs were also the highest in these 2 regions, at 11% for each, compared to just 8% in north Queensland and 6% in the rest of Australia.

Figure 7.18: Proportion of cost categories for all home and contents insurance, by region, 2022–23



Source: ACCC analysis of data obtained from insurers.

Reinsurance cost

Insurers purchase reinsurance to protect themselves against large losses from catastrophic events. Reinsurance costs are the largest cost to insurers after net claim costs. The Northern Australia Insurance Inquiry found that they were a significant factor contributing to higher premiums in northern Australia.[293] In calculating the technical premium, insurers take into account the net cost of reinsurance – that is, the reinsurance premium less expected reinsurance recoveries from the reinsurers.

Figure 7.19 shows reinsurance costs and recoveries from 2010–11 to 2022–23 for all home and contents insurance policies written in northern Australia. For the insurers in our sample, reinsurance costs increased steeply from $138 million in 2010–11 to $269 million in 2012–13, in real terms. From this point on, the reinsurance cost stayed at a similar level, remaining in the range of about $260–280 million per year until 2018–19, and then fell slightly to $214 million in 2019–20. Reinsurance costs thereafter increased slightly each year up until 2022–23, to around $240 million.[294] When interpreting this trend, it should be noted that insurers may not necessarily be purchasing the same level or type of cover each year. If insurers choose to retain more risk, this may result in lower reinsurance costs, if rates are comparable to previous years.

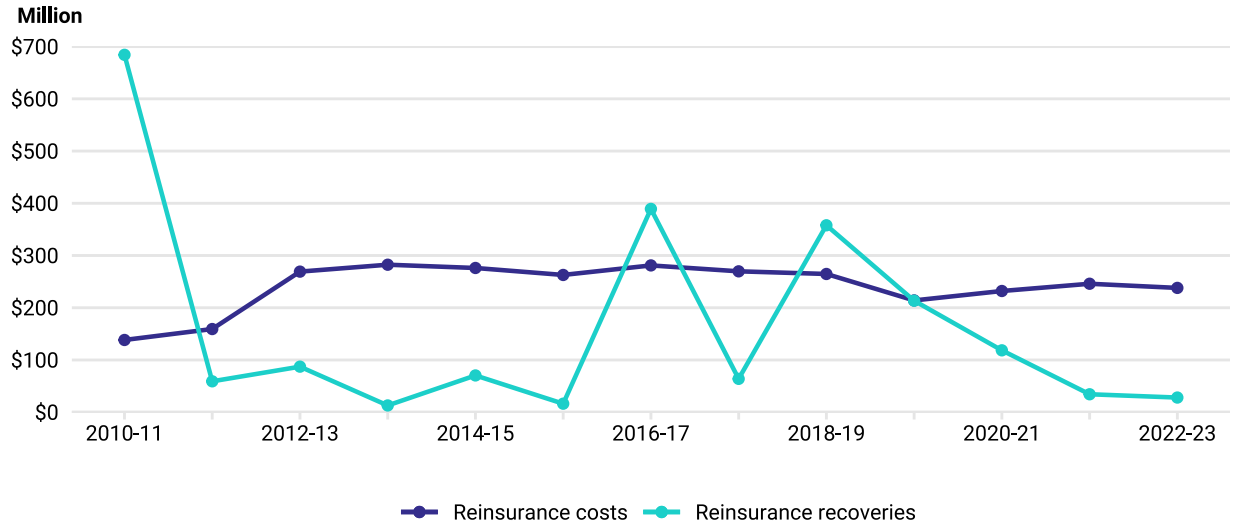
Insurers in our sample recovered the largest inflation adjusted amount ($684 million) from reinsurers in 2010–11, followed by $389 million in 2016–17 and $358 million in 2018–19. The spikes in reinsurance recoveries are due to Cyclone Yasi, Cyclone Debbie and the Townsville floods, which caused reinsurance recoveries to exceed reinsurance expenses in northern Australia.[295] The chart illustrates that, in recent years, insurers continued to incur reinsurance costs but have had minimal recoveries due to few significant events during this period.

293 ACCC, *NAII final report*, p 70.

294 It is to be noted that the data prior to 2019–20 were collected for NAII final report. The data for 2019–20 and 2020–21 does not include one insurer which was subsequently acquired in 2021–22 by another insurer included in the data.

295 ACCC, *NAII final report*, p 101.

Figure 7.19: Reinsurance costs and recoveries for all home and contents insurance, northern Australia, 2010–11 to 2022–23, adjusted for inflation



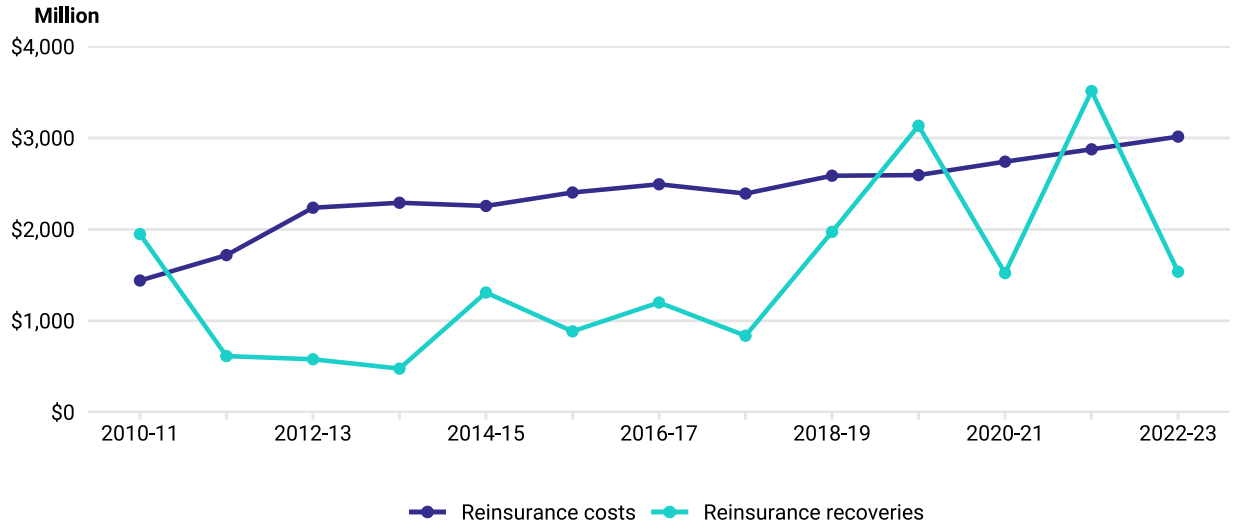
Source: ACCC analysis of data provided by insurers.

Figure 7.20 below shows reinsurance costs and recoveries from 2010–11 to 2022–23 for all home and contents insurance policies for the whole of Australia. In contrast across Australia, reinsurance costs have generally increased steadily from 2010–11 to 2022–23, in real terms, for the insurers in our sample. Reinsurance costs increased by approximately 5% to 6% per year between 2020–21 and 2022–23. Reinsurance costs for 2022–23 for all home and contents insurance policies totalled $3.01 billion, for the insurers in our sample. As noted above, when interpreting this trend it should be noted that insurers may not necessarily be purchasing the same level or type of cover each year. If insurers choose to retain more risk, this may result in lower reinsurance costs if rates are comparable to previous years.

Insurers in our sample recovered the largest inflation adjusted amount ($3.51 billion) from reinsurers in 2021–22, followed by $3.13 billion in 2019–20. The spikes in reinsurance recoveries were likely due to the eastern Australia floods in 2022, and the 2019–20 bushfires across a number of states and territories. Between 2011–12 and 2018–19, reinsurance costs exceeded reinsurance recoveries.

When considering how trends in Figures 7.19 and 7.20 compare, these should be interpreted with caution, as insurers have relied on a range of methodologies and assumptions to allocate financial data between regions. We will monitor outcomes in these figures closely in future years.

Figure 7.20: Reinsurance costs and recoveries for all home and contents insurance, Australia, 2010–11 to 2022–23, adjusted for inflation

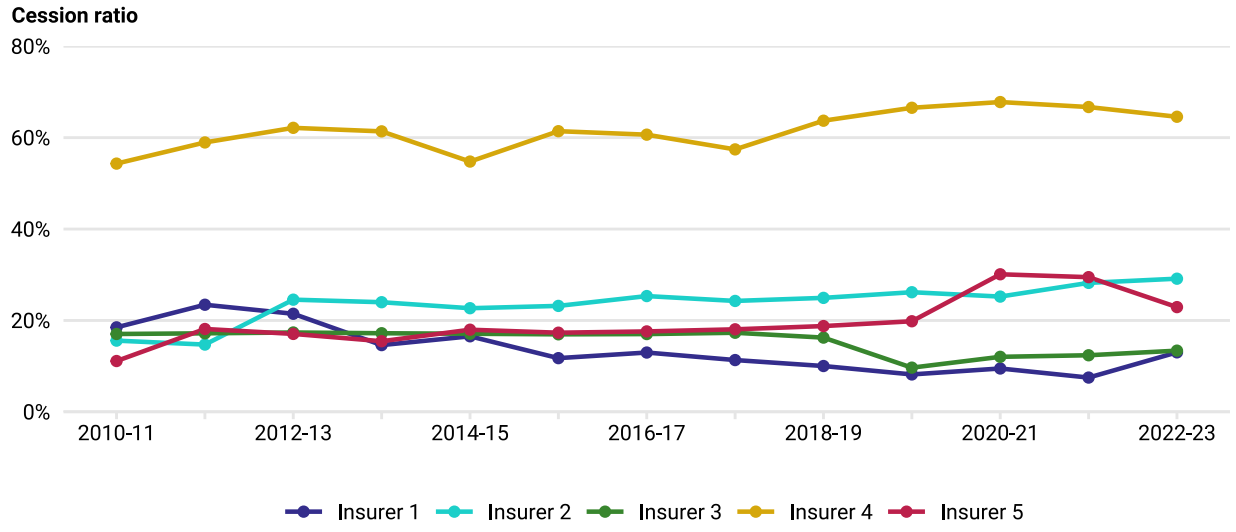


Source: ACCC analysis of data provided by insurers.

Figure 7.21 below shows the cession ratio of the insurers in our sample across Australia, for the period 2010–11 to 2022–23. The cession ratio is the reinsurance expense divided by gross earned premium. It gives an indication of how much risk insurers retain or pass on to reinsurers. The higher the cession ratio, the higher the risk passed on by the insurer to the reinsurer and vice versa. Section 5.3 discusses some of the changes insurers have made to their reinsurance programs in 2022–23, and their stated reasons for amendment.

There is a wide range in the cession ratios across insurers, reflecting the different risk appetites and reinsurance programs of each insurer. Insurer 5 had a recent jump in its cession ratio, with a high of 30% in 2020–21, but most prior years were in the 15% to 19% range. Insurer 1's cession ratio was generally decreasing from a high of 23% in 2011–12, to a low of 8% in 2021–22. Insurer 2 maintained a fairly steady cession ratio between 23% and 30% since 2012–13. On the other hand, Insurer 4 maintained its cession ratio in the range of 54% to 68% across the period studied. This was by far the highest cession ratio observed, and is clearly reflective of a very different reinsurance strategy to other insurers studied. The majority of insurers had cession ratios below 40%, suggesting that these insurers retained most of the risk instead of passing it on to reinsurers.

Figure 7.21: Cession ratio for all home and contents insurance, by insurer, Australia, 2010–11 to 2022–23



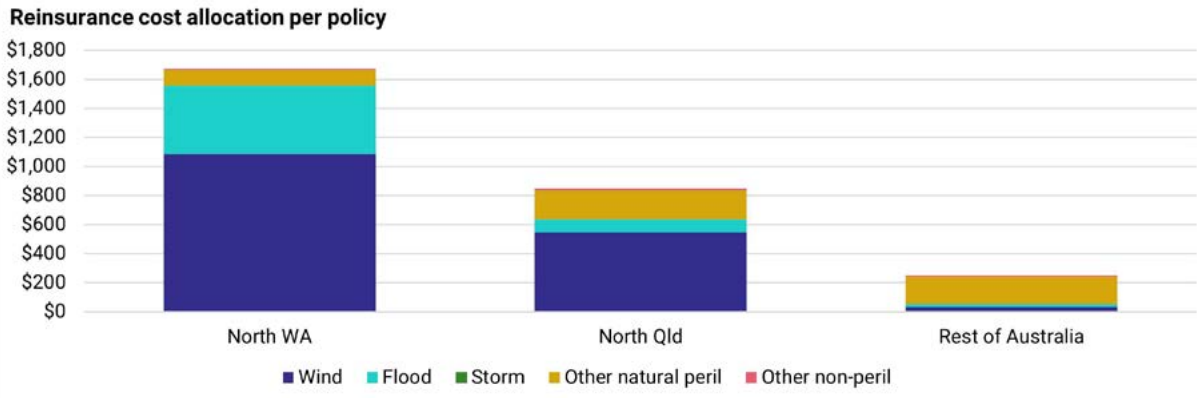
Source: ACCC analysis of data provided by insurers.

Figure 7.22 below illustrates which perils contributed the most to reinsurance costs on an average policy by region. The analysis presented here represents the apportionment of reinsurance costs by peril against the average retail premium, and is distinct from actual or realised reinsurance costs as presented in Figure 7.20. The Northern Territory was excluded from this analysis due to insufficient data.

As shown, north Western Australia had the highest average reinsurance cost of $1,672 per policy, driven predominantly by cyclone-related wind ($1,088) as well as flood ($470). Policies in north Queensland had the second highest average reinsurance cost, comprising $850 of the average premium. Cyclone-related wind was the main contributor to the reinsurance cost ($546) in north Queensland.

Reinsurance costs were lowest in the rest of Australia, comprising $250 of the average premium. In contrast to northern Australia, cyclone-related wind, along with flood, made up a very small proportion of overall reinsurance costs allocated to premiums for the rest of Australia, reflecting the much smaller or negligible risk of cyclones currently faced in those regions compared to northern Australia.

Figure 7.22: Reinsurance cost components allocated to the average retail premium, for all home and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

8. Strata insurance

In the NAII final report, we found that some strata properties in northern Australia faced acute insurance availability and/or affordability issues. These properties tended to be large (over $5 million sum insured), older (particularly for those built before 1985) and located in close proximity to the coastline.[296] The concerns facing owners of strata properties are exacerbated by the mandatory nature of strata insurance, and who cannot opt to self-insure.

As discussed in Section 6.2.2, state and territory legislation in each of Queensland, Western Australia and the Northern Territory imposes a legal requirement for strata titled properties to insure common property, buildings and assets for their full replacement or reinstatement value. Whilst the respective legislative requirements across these 3 jurisdictions differ slightly, it is true as a broad generalisation that there is a mandatory requirement for insurance to be held. There are very limited exemptions to these requirements for full insurance, particularly in Queensland and Western Australia. While these requirements ensure that strata properties have protection in the event of a disaster, it does mean that these customers are particularly exposed to the effect of price increases.

Strata insurance covers loss and damage caused to strata title properties, and the type of coverage will depend on the nature of the strata property. For instance, coverage for a free-standing property which is part of a strata complex may be limited to common areas. Strata insurance does not typically provide coverage for personal items and contents, so residents of strata complexes generally hold their own, separate contents insurance.[297]

In this chapter we look at the prices and a breakdown of premiums for strata insurance. The figures presented in this chapter show information up until 30 June 2023. As only a few insurers had joined the pool at the time, our analysis of the pool's effect is necessarily limited. We anticipate being able to present more direct analysis of the pool's effect in future reports once a greater number of insurers have been in the pool for a longer period.

Similar to Chapter 7, we used our information gathering powers to obtain policy level data, policy and claims summary information and financial information from select insurers. Where appropriate, we have combined policy and claims summary information and financial information with information collected in our previous Northern Australia Insurance Inquiry. We note that policy level data is as at 30 September 2022, while policy and claims summary information and financial information was collected on a financial year basis. As such, while the periods overlap, there may be slight differences in values between figures. Where applicable, we have noted these differences in our analysis.

Further information on our data collection, methodology, and refinements can be found in Appendix A. We will continue to build upon our data collection in future reports.

The analysis reported in this chapter is for entire strata complexes and does not account for the number of dwellings covered.[298] There can be wide variations in average annual premiums for strata policies, depending on the type and size of strata title property insured in the relevant area. They also do not include additional fees that may be applied by an insurance broker or strata manager for arranging insurance.

296 ACCC, *NAII final report*, p 419.

297 ACCC, *First insurance monitoring report*, pp 35–36.

298 Properties covered under industrial special risks insurance are excluded. Industrial special risks is a policy which covers key events and is a business and property insurance product generally for assets valued over $5 million. We have not undertaken analysis of industrial special risks in this report, but it may be included in future reports.

In Section 8.1, we provide the average premiums paid for strata insurance by different regions and over time. We also analyse average premiums by sum insured, average premiums by excess, and average premiums by excess and sum insured.

In Section 8.2, we provide a breakdown of retail premiums for strata insurance into the various components that contribute to the insurance premiums charged to the policyholder.

Overall, we find that premium prices for strata insurance have increased year on year. Prices remained particularly elevated for regions in northern Australia, even when sum insured and excess levels were accounted for. Additionally, higher excess levels tended to be selected in northern Australian regions, likely reflecting attempts by customers in those areas to reduce the high premium prices they face.

8.1 Prices of strata insurance

This section provides analysis on strata insurance prices. Similar to Chapter 7, we look at strata insurance prices in several ways: average premiums and the range of premiums (Section 8.1.1), premiums per $100,000 sum insured (Section 8.1.2), premiums by excess (Section 8.1.3), and premiums by sum insured and excess (Section 8.1.4).

In addition to providing average values, we have also included box plots showing the range of premiums, where appropriate. This allows for a deeper look at the prices paid by a wider range of strata policyholders, including larger and more complex dwellings. We have also split some of our analysis into lower, medium, and higher sum insured strata, using sum insured as a proxy to better understand pricing for different sizes of strata complexes. We will continue these analyses in future reports to assess changes in pricing outcomes and pool impacts over the longer term.

We provide ranges of pricing outcomes in the form of box plots where appropriate. Due to some extreme values, the top and bottom 5% are not displayed in box plots to aid readability of the figures. As such, they may not necessarily reflect the individual experiences of particular policyholders, and more recent changes in premiums. We will continue to closely watch broader pricing outcomes throughout our monitoring.

8.1.1 Premiums paid for strata insurance

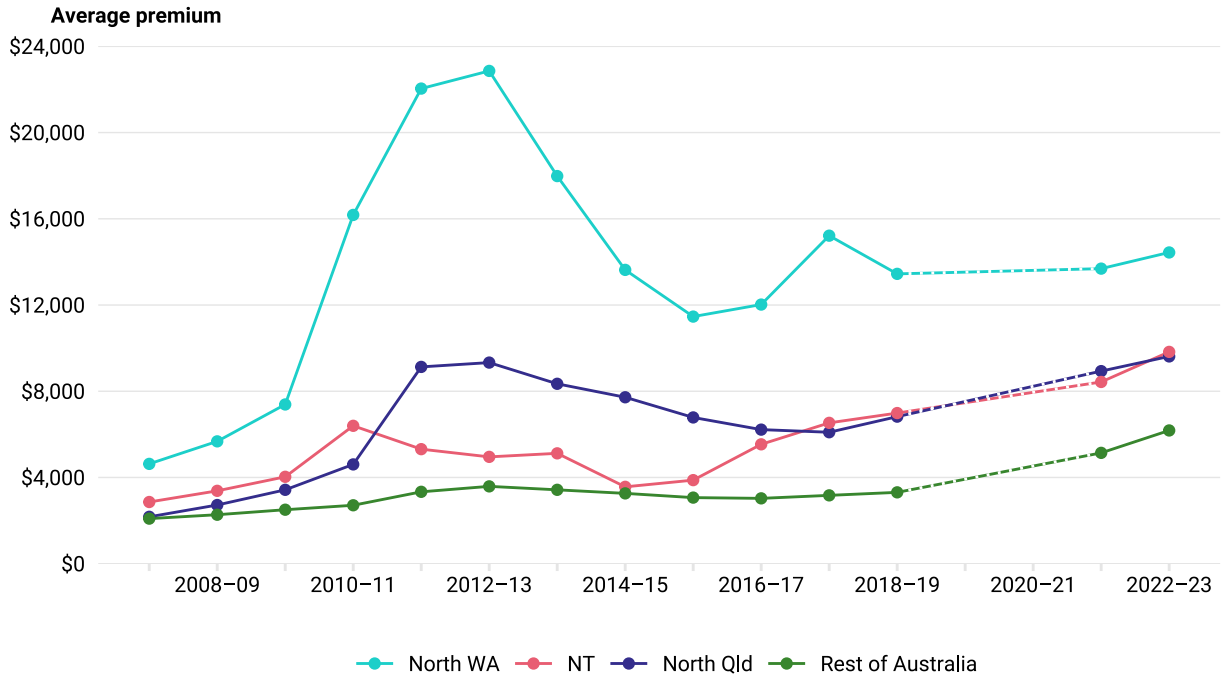
This section analyses the premiums paid by policyholders for strata insurance. The average premiums presented are the mean value of the premiums for strata insurance products supplied by insurers at a policy, postcode or regional level. They include GST, stamp duty and applicable levies. They represent actual prices paid by consumers for insurance products, including any commissions built into premiums, but do not include additional fees that may be applied by an insurance broker or strata manager for arranging insurance. They do not include quoted premiums that were not ultimately taken up by consumers due to various reasons, including unaffordability.

Mean figures do not show the range of outcomes within regions. Where relevant in this section, we also present information on median results and show the range of strata insurance premiums paid by policyholders.

Figure 8.1 below shows that average premiums for strata insurance remained high in northern Australia and increased in 2022–23 across all regions, in nominal terms. As noted in Chapter 7, these nominal results may reflect the lived experience of policyholders when they compare the change in their premiums year on year. The rest of Australia experienced the largest year on year percentage increase of 20% with an average of $6,181. The Northern Territory experienced an increase of 17% between 2021–22 and 2022–23 (from $8,431 to $9,826), while north Queensland experienced an 8% increase (from $8,934 to $9,615). North Western Australia experienced an increase of 5% in

nominal terms, with average premiums increasing from $13,688 to $14,439. The larger percentage increase for the rest of Australia may reflect the impact of significant disasters in southern parts of the country in 2022. However, average premiums remained much higher in northern Australia.

Figure 8.1: Average premiums for strata insurance, by region, 2007–08 to 2022–23

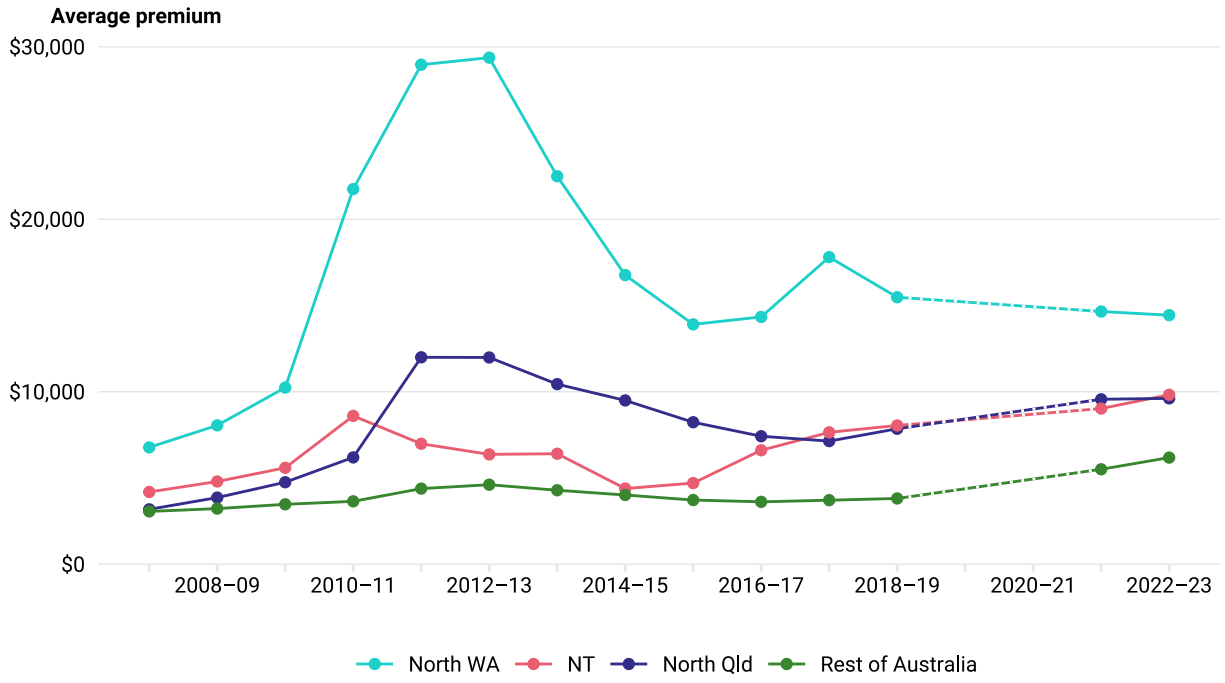


Source: ACCC analysis of data obtained from insurers.

As with Chapter 7, much of our price trend data is presented over a long period of time. Accordingly, the rest of this section presents figures in real terms (to 2022–23 dollars) where appropriate. This means that reported premiums for previous years have been adjusted to remove the effect of general price inflation on price trends.

Figure 8.2 below shows that average premiums for strata insurance in 2022–23 increased in some regions, in real terms. The rest of Australia experienced the largest increase of 12% (from $5,503 to $6,181), although the region continued to have the lowest average premiums. The Northern Territory experienced an increase in average premium of 9% (from $9,024 to $9,826, while north Queensland had an increase of 1% (from $9,562 to $9,615). North Western Australia experienced a slight decrease in real terms of 1% (from $14,650 to $14,439), although average premiums in the region remained the highest. Average premiums in northern Australia remained higher than the rest of Australia.

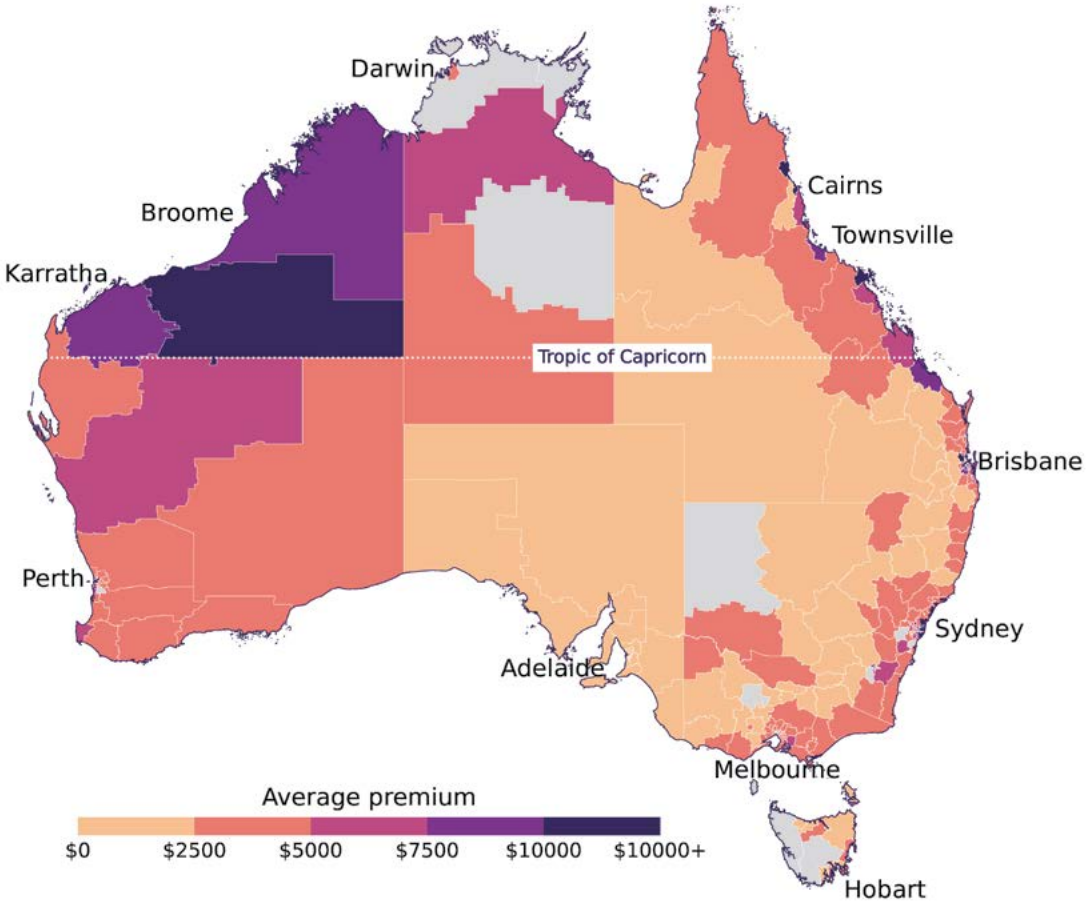
Figure 8.2: Average premiums for strata insurance, by region, 2007–08 to 2022–23, adjusted for inflation



Source: ACCC analysis of data obtained from insurers.

Figure 8.3 below shows that the north Western Australia regions generally had very high average premiums for strata insurance products. There were also high premium regions in the Northern Territory, and some areas along the eastern Queensland coast. Regions shown as grey were unable to be shown due to insufficient data to calculate reliable averages.

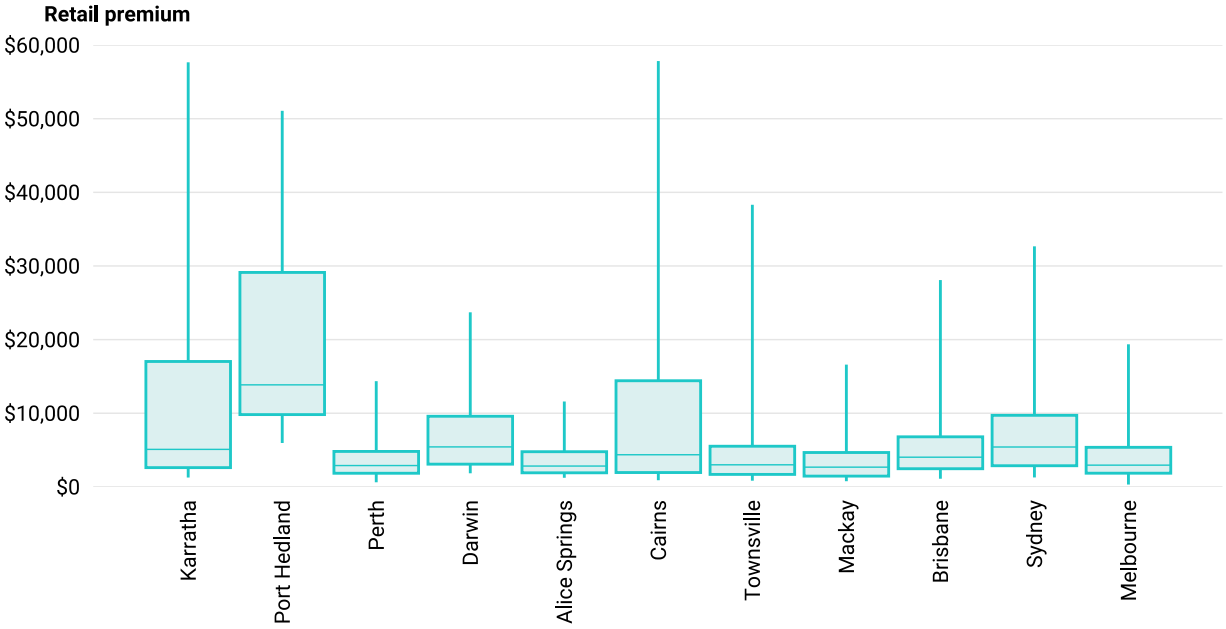
Figure 8.3: Average premiums for strata insurance, by Statistical Area Level 3, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 8.4 below shows the distribution of strata premiums by select cities and towns. Port Hedland had the highest median premium of $13,855, followed by Darwin ($5,428), Sydney ($5,411), Karratha ($5,089) and Cairns ($4,361). There was generally a large spread of premiums in each city and some extremely high retail premiums. This was particularly pronounced in Port Hedland, Karratha and Cairns, with the top 5% of policyholders paying over $51,072, $57,659, and $57,829 respectively. This large spread could be due to a number of factors including the diversity in size of strata complexes, and risk profiles in those cities. We note that, while northern Australia generally pays more for strata insurance on average, outcomes vary for different cities across the north of the country. Again, this likely reflects differences in the types of strata complexes being insured.

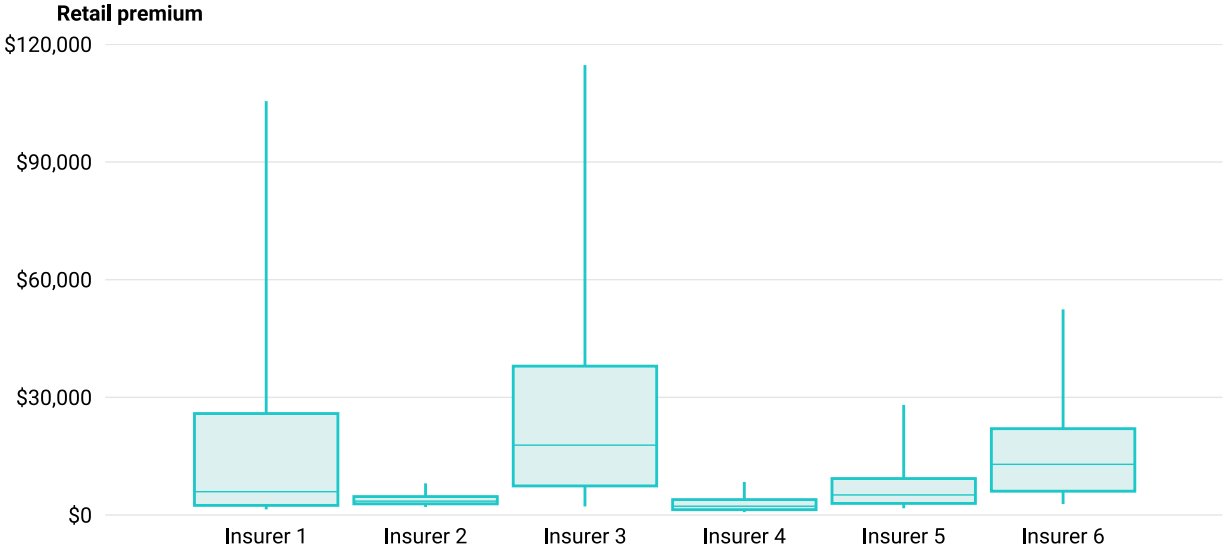
Figure 8.4: Distribution of retail premiums for strata insurance, select cities and towns, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 8.5 below shows the distribution of strata premiums by insurer in northern Australia for select insurers. The median prices varied greatly by insurer, ranging from $2,246 to $17,812. There were also large differences in premiums within each insurer, particularly those with higher median premiums. The differences between insurers are likely due to differences in underwriting guidelines.[299] Chapter 6 discusses the common underwriting restrictions that insurers use to manage risk exposure.

Figure 8.5: Distribution of retail premiums for strata insurance, by insurer, northern Australia, 2022



Source: ACCC analysis of data obtained from insurers.

299 ACCC, *NAII final report*, p 421.

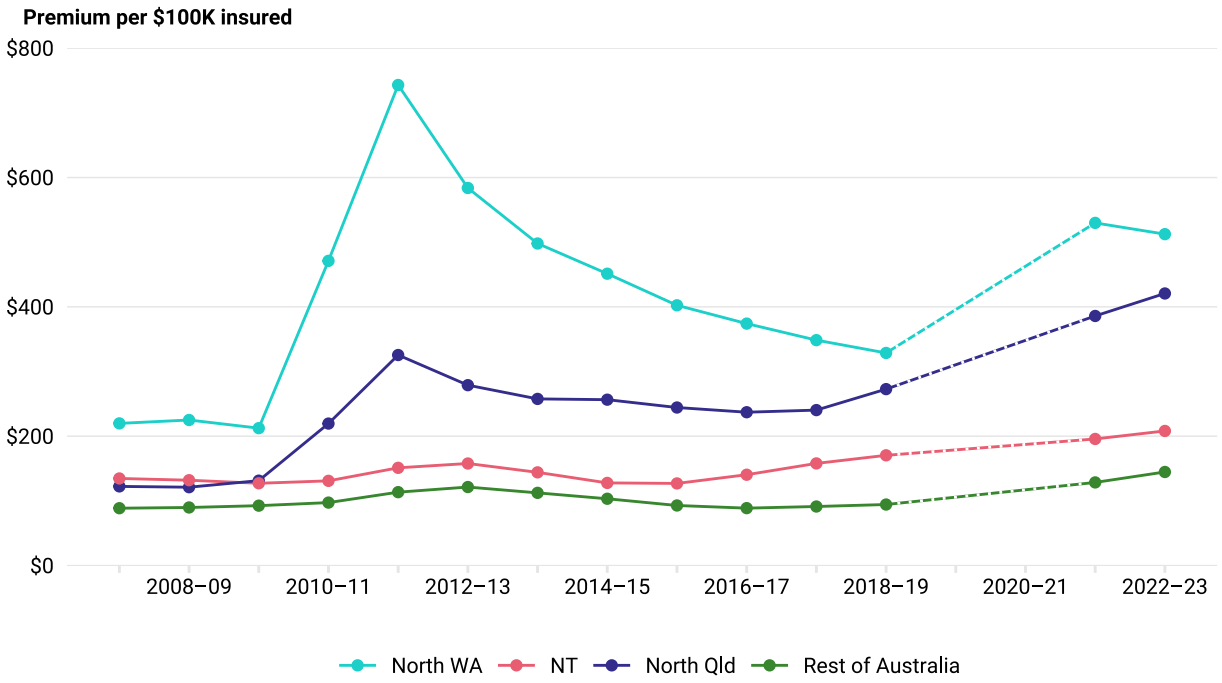
8.1.2 Premiums by sum insured

This section presents analysis on premiums per $100,000 sum insured. A premium per $100,000 sum insured measure, in contrast to the above Section 8.1.1, accounts for differences in the amount a property is insured for, between policies and areas. As noted earlier, there can be wider variations in the average annual premiums for strata policies, depending on the type and size of strata title property insured in the relevant area. However, examining premiums per $100,000 sum insured can, to an extent, take into account differences in the size of insured properties (see Section 7.1.2. for further discussion on the impact sums insured have on premiums).[300]

Aside from north Western Australia, all regions saw an increase in average premiums per $100,000 sum insured for strata insurance over the last year. Figure 8.6 below shows that north Queensland had an average premium per $100,000 sum insured of $421 in 2022–23, an increase of 9% year on year. North Western Australia continued to have the highest premium per $100,000 sum insured at $512, though this was a 3% decrease from the previous year. The average premium per $100,000 sum insured for the Northern Territory was $208, a 6% increase from the previous year. The average premium per $100,000 sum insured for the rest of Australia was the cheapest at $145, a 13% increase from the previous year.

It is evident from the time series in Figure 8.6 that, irrespective of the year, consumers in northern parts of Australia have paid more for strata insurance even when the sum insured is factored into the average premium price. Prices for strata insurance per $100,000 sum insured in north Queensland and north Western Australia are around 3 times that paid by those outside northern Australia.

Figure 8.6: Average premiums per $100,000 sum insured for strata insurance, by region, 2007–08 to 2022–23

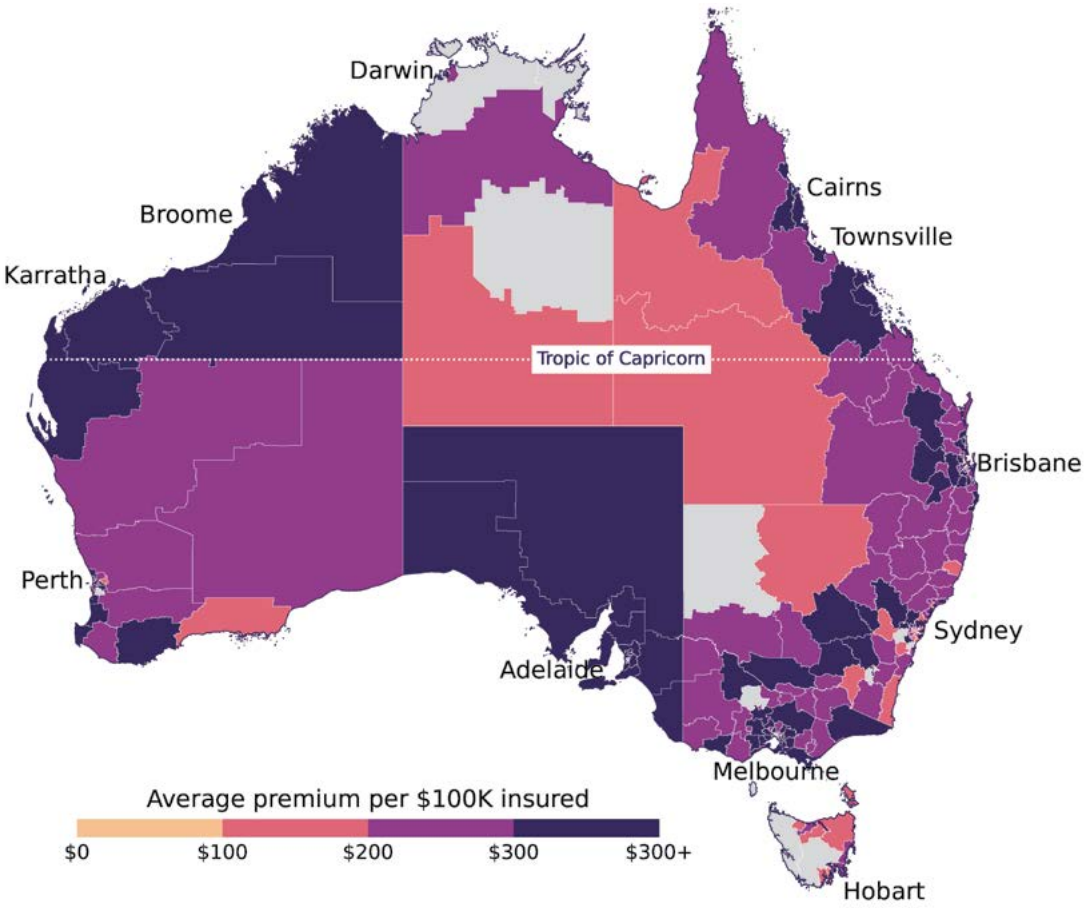


Source: ACCC analysis of data obtained from insurers.

Figure 8.7 below shows that the average premium for strata insurance per $100,000 sum insured for north Western Australia was the most expensive amongst the northern regions (over $300). Most of South Australia was also in the highest (over $300) average premium per $100,000 sum insured band. Most coastal locations in north Queensland paid more than $200 per $100,000 sum insured.

300 ACCC, *NAII final report*, p 51.

Figure 8.7: Average premiums per $100,000 sum insured for strata insurance, by Statistical Area Level 3, 2022

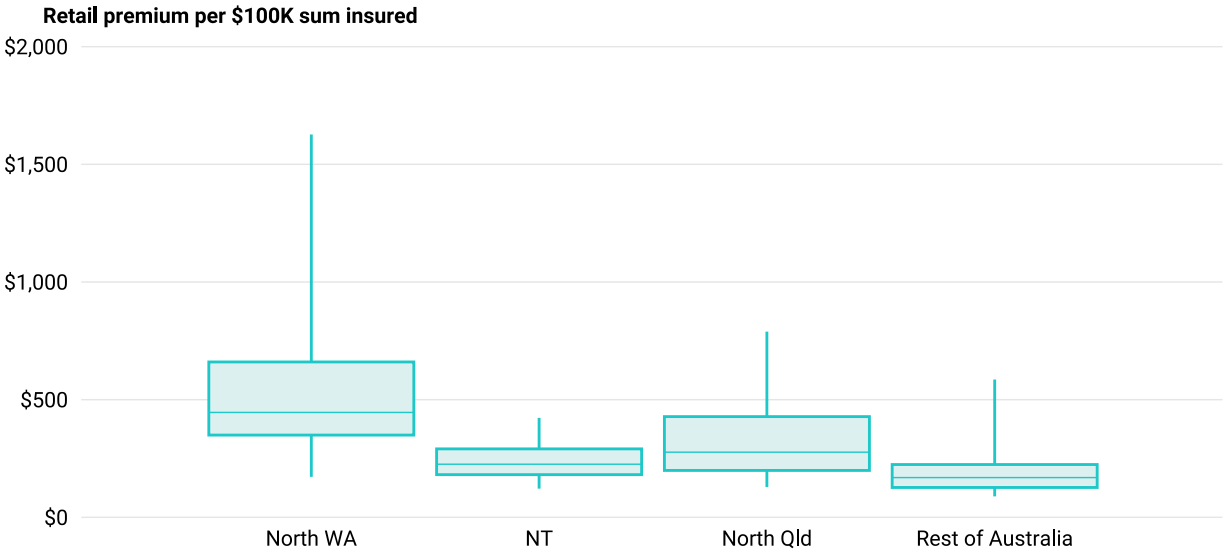


Source: ACCC analysis of data obtained from insurers.

Figure 8.8 below shows that north Western Australia continued to have the highest median premium per $100,000 sum insured amongst the northern regions for strata insurance ($446). North Queensland had the second highest median ($277). The Northern Territory had a median of $226 and the rest of Australia had a median of $169. The figure shows that, while strata insurance premiums were generally higher in all northern Australian regions compared to the rest of Australia, premiums in north Western Australia in particular were higher and more variable.

Only 34% of policyholders in areas outside northern Australia paid more than $200 per $100,000 sum insured, compared to 73% across northern Australia.

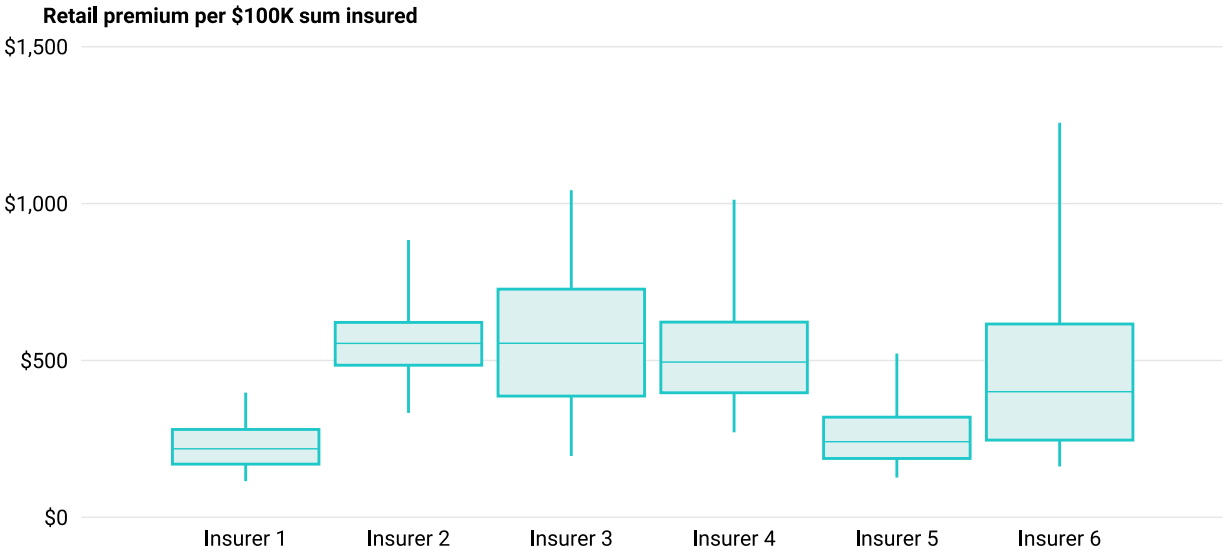
Figure 8.8: Distribution of retail premiums per $100,000 sum insured for strata insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 8.9 below shows that there was high variability across all insurers for strata insurance prices per $100,000 sum insured in northern Australia. Insurer 1 had the lowest median ($219), while Insurers 2 and 3 had the highest medians ($554 and $555, respectively). Some insurers also had a very large spread of premiums per $100,000 sum insured. The differences in the median and range of premium prices between insurers could be due to different customer acquisition strategies or a more selective customer retention strategy, rather than indicative of potential savings for particular customers.[301] While the values presented are for northern Australia generally, insurers may choose to selectively target certain locations or types of risk within that region (availability of insurance is discussed further in Chapter 6).

Figure 8.9: Distribution of retail premiums per $100,000 sum insured for strata insurance, select insurers, northern Australia, 2022



Source: ACCC analysis of data obtained from insurers.

301 ACCC, *NAII final report*, p 29.

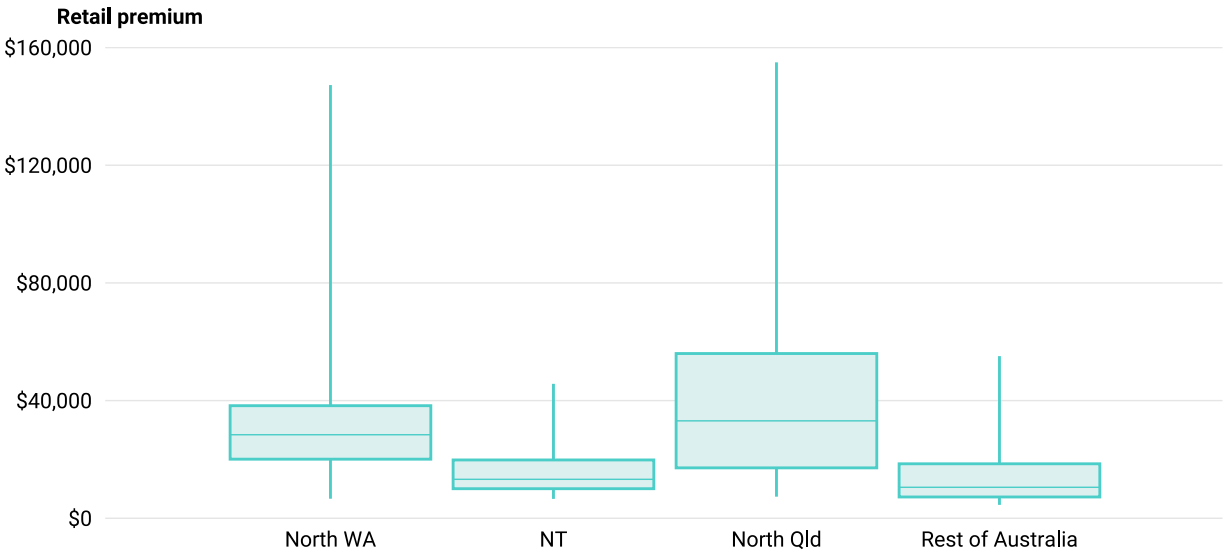
The following figures below (Figures 8.10, 8.11 and 8.12) show the spread of premiums paid by policyholders in 2022, split by higher sums insured, medium sums insured and lower sums insured strata policies. As discussed earlier, there can be wide variations in average annual premiums for strata policies, depending on the type and size of strata title property insured in the relevant area. By splitting strata into higher, medium and lower sums insured, we can better understand outcomes for different strata groups.

The bounds used are as follows: higher (over $4 million sums insured), medium (between $2 million and $4 million), and lower ($2 million and under). Further information on how the bounds were selected can be found in Appendix A. To aid the readability of the charts, the top and bottom 5% are not displayed due to extreme values.[302]

Broadly, across all sizes of strata, premiums paid in northern Australia were higher and had a greater spread than for the rest of Australia. However, there were some differences around which the northern Australian region paid the highest premiums by strata size, as discussed below.

Figure 8.10 below illustrates the spread of premiums paid by policyholders in 2022 for higher sums insured strata. The figure shows that policies in north Queensland had the highest median prices ($33,118) for higher sum insured strata insurance, closely followed by north Western Australia ($28,393). The Northern Territory and the rest of Australia showed similar values for median premiums, at $13,245 and $10,535 respectively. The range of premiums paid in north Queensland was greater than the other regions.

Figure 8.10: Distribution of retail premiums for strata insurance, sums insured over $4 million, by region, 2022

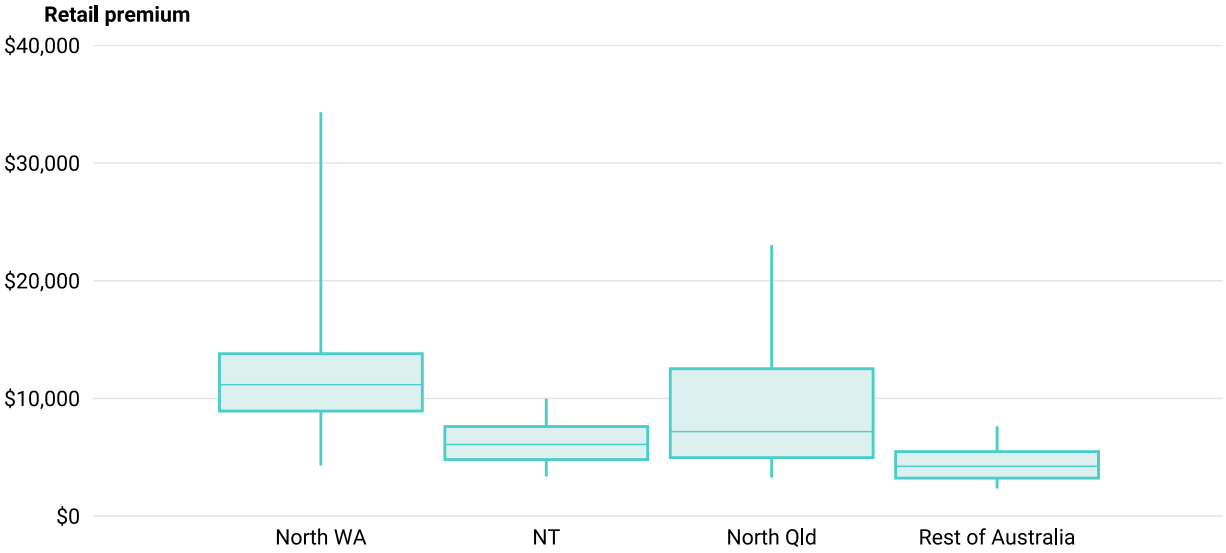


Source: ACCC analysis of data obtained from insurers.

In contrast, Figure 8.11 (below) shows the north Western Australia region had the highest median premiums ($11,172) for medium sum insured strata insurance, followed by north Queensland ($7,183). The Northern Territory and the rest of Australia had median premiums of $6,092 and $4,240 respectively.

302 We note that values not displayed in this figure are actual premiums faced by policyholders and are only removed for the purposes of clearly illustrating the experience of most policyholders. Values not displayed are included in calculations of the mean. Further information on our methodology is provided in Appendix A.

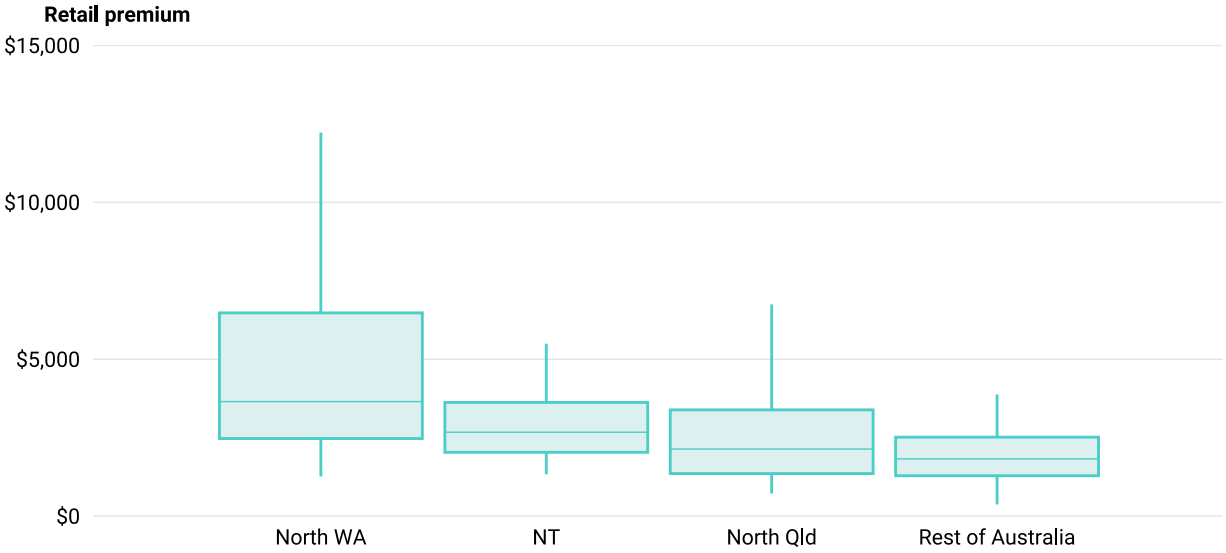
Figure 8.11: Distribution of retail premiums for strata insurance, sums insured between $2 million and $4 million, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Finally, Figure 8.12 below shows that the north Western Australia region had the highest median premiums ($3,650) and spread for lower sum insured strata insurance than the other regions. North Queensland ($2,138) and the Northern Territory ($2,675) also exhibited higher-priced medians compared to the rest of Australia ($1,825).

Figure 8.12: Distribution of retail premiums for strata insurance, sums insured under $2 million, by region, 2022



Source: ACCC analysis of data obtained from insurers.

8.1.3 Premiums by excess

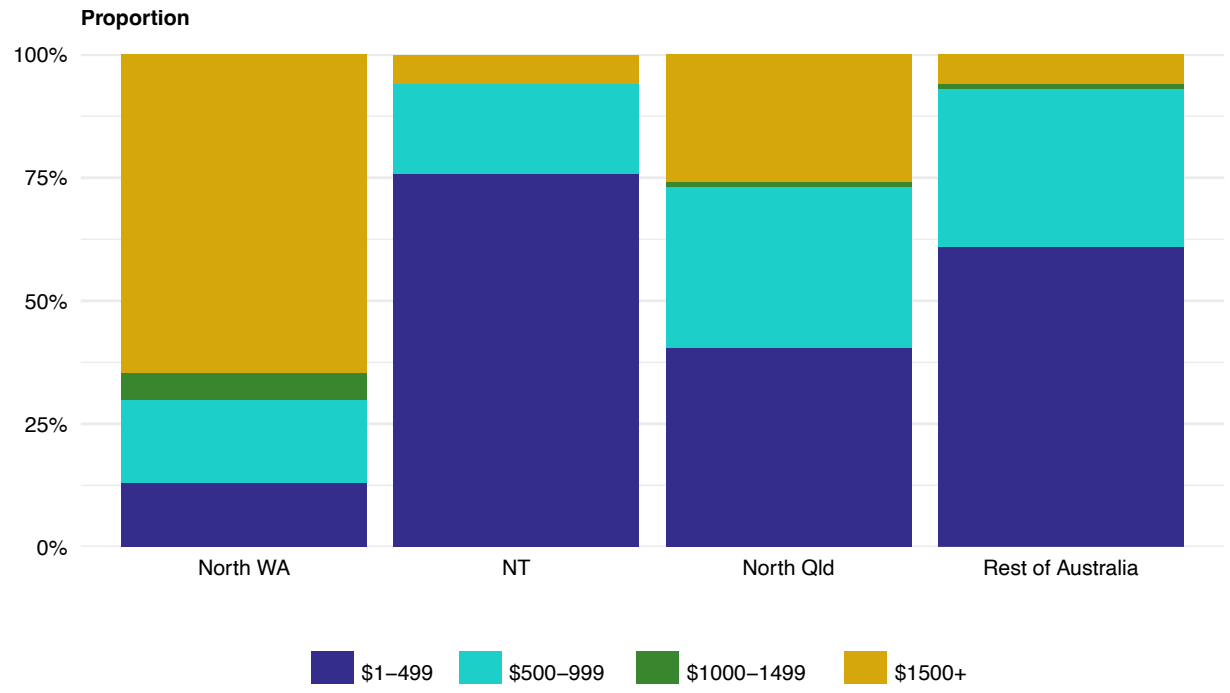
This section presents analysis on the excess levels selected by policyholders, and average premiums when excess is accounted for. An insurance excess is the amount of money a customer is required to pay towards the costs of a claim they make, and is one of the limited options open to the policyholder to adjust the premium rate of their policy. The higher the excess a customer selects, the lower their premium will be, but equally the overall value of the policy is lower as it is less economical to make a smaller claim. Therefore, it is important to consider the excess levels when interpreting premium levels and movements (see Section 7.1.3. for a detailed explanation on the relationship between excesses and premiums).

Figure 8.13 below shows that excess levels in north Western Australia were on average considerably higher than in the other regions, including north Queensland. In this region, 65% of policies had an excess of $1,500 or more, compared to 26% in north Queensland and less than 6% in the Northern Territory and rest of Australia. Only 13% of policies in north Western Australia had an excess below $500, compared to 61% for the rest of Australia. The Northern Territory had the majority (76%) of its strata insurance policies with excesses between $1 and $499.

Overall, the differences in these excess levels are similar but more pronounced compared to home and contents insurance products, where the excess levels in north Western Australia and north Queensland were also considerably higher than the Northern Territory and the rest of Australia (see Section 7.1.3).

As shown in Figures 8.6 and 8.8 above, north Western Australia and north Queensland paid higher premiums per sum insured than the other regions. A possible explanation for these observations is that policyholders from more expensive regions may be choosing higher excesses to keep premiums lower than they would otherwise be with smaller excesses.

Figure 8.13: Proportions of excess brackets for strata insurance, by region, 2022

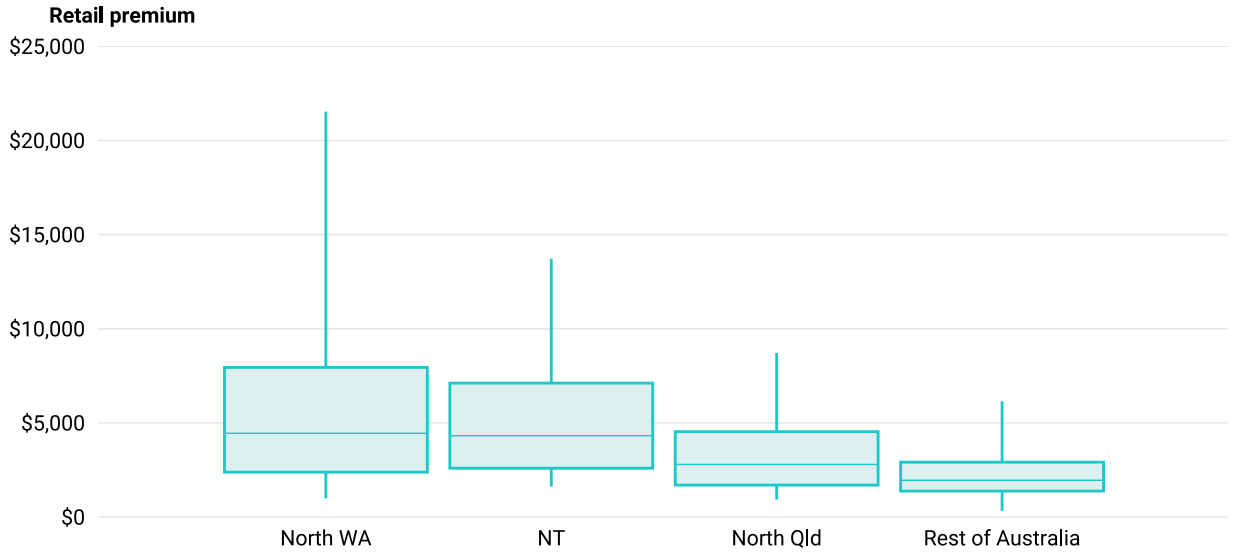


Source: ACCC analysis of data obtained from insurers.

Figure 8.14 below shows that, when looking at strata insurance policies with 'typical' excess amounts (between $100 and $500), north Western Australia and the Northern Territory had higher medians ($4,449 and $4,318, respectively) than north Queensland ($2,791) and the rest of Australia ($1,951).

North Western Australia also had a large spread of values. Importantly, the 'typical' excess band of $100 to $500 for strata policies captures the most common excess values chosen across Australia overall (see Figure 8.13). We note this is not necessarily reflective of the 'typical' excess band chosen by policyholders in northern Australia who are more often choosing excess values greater than $500 (see Figure 8.13).

Figure 8.14: Distribution of retail premiums for strata insurance, excesses between $100 and $500, by region, 2022



Source: ACCC analysis of data obtained from insurers.

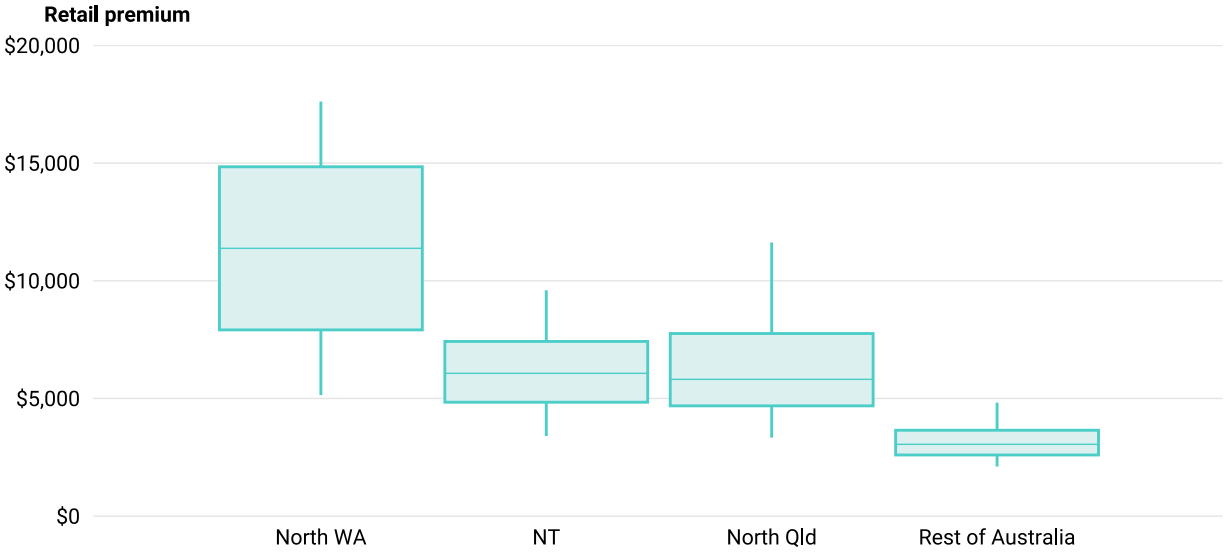
8.1.4 Premiums by excess and sum insured

In this section, we present analysis on the average premiums paid for strata insurance within select sums insured and excess levels, and see the extent of any differences in outcomes when both these variables are controlled for.

We aim to compare average premium outcomes by insurer and between regions when 'typical' sum insured and excess levels are selected. It should be noted that the sum insured and excess bands selected are based on what is typical across all strata insurance policies. However, they may not be the typical or most common sum insured or excess levels for a particular insurer or a particular region.

Figure 8.15 below shows the premium distribution for strata insurance across regions for 'typical' excesses between $100 to $500 and sum insured values of $2 million to $4 million. Even when excess levels and sum insured values are held to a 'typical' level, average premiums were still higher in northern Australia. The median retail premium was highest in north Western Australia $11,379, followed by the Northern Territory ($6,067), north Queensland ($5,813), and the rest of Australia ($3,051). The northern regions also had the greatest spread in retail premium prices.

Figure 8.15: Distribution of retail premiums for strata insurance, excess between $100 and $500, sums insured between $2 million and $4 million, by region, 2022



Source: ACCC analysis of data obtained from insurers.

8.2 Breakdown of insurance premiums

This section provides a breakdown of retail premiums and examines insurer costs for strata insurance products in different regions across Australia. The breakdown of retail premiums for strata insurance products in northern Australia are examined in Section 8.2.1, while insurer costs are examined in Section 8.2.2.

8.2.1 Breakdown of retail premiums

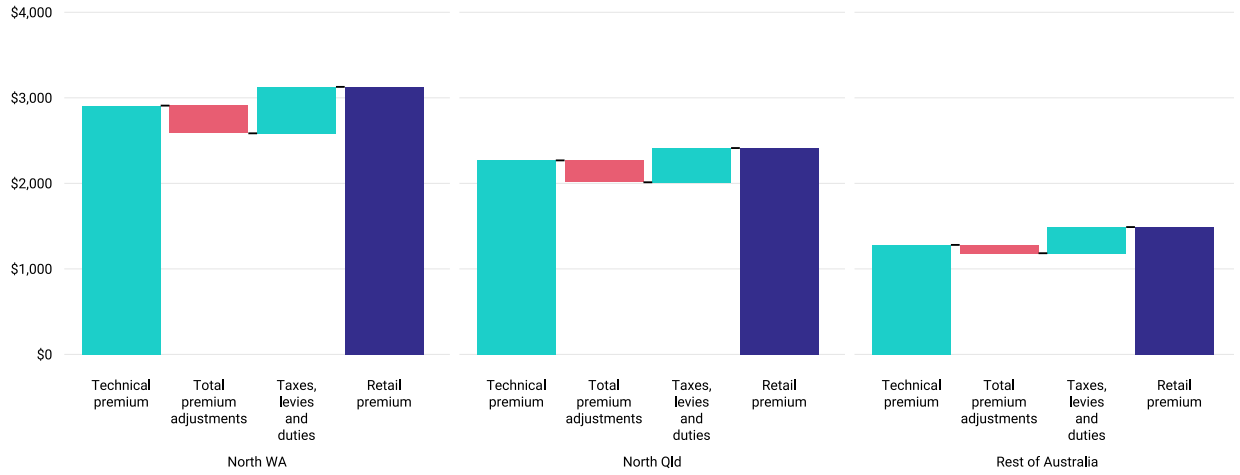
Similar to home insurance, we have broken strata insurance retail premiums into the technical premium, premium adjustments, and taxes and levies as outlined in Chapter 7.

Figure 8.16 below shows the average result of each of these steps to calculating the retail premium for strata insurance in northern Australian regions for policies with a sum insured of less than $2 million, as at September 2022.[303] We note that only records with complete (in other words, not missing) technical premium, premium adjustments, taxes and levies and retail premium values were included in the below analysis. This means that the figures represent a large, but not complete, proportion of policies from the data we obtained.[304] We have excluded the Northern Territory from this analysis due to insufficient complete data records.

303 Due to data limitations, we were unable to present comparable breakdown information for higher sums insured (i.e. policies for medium and high value strata policies). The breakdown of retail premiums may be different for those properties.

304 The proportion of policies with complete data by region is as follows: north Queensland (82.3%), north Western Australia (80.8%), and rest of Australia (40.1%).

Figure 8.16: Average retail premium breakdown for strata insurance, sums insured under $2 million, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Note: Only complete records containing technical premium, premium adjustments, taxes and levies and retail premium values have been included in this analysis.

North Western Australia had the highest average technical premium for a strata policy with a sum insured up to $2 million at $2,909, followed by north Queensland at $2,269. The rest of Australia had the lowest average technical premium of $1,280. Higher average technical premiums in northern regions is reflective of the higher expected claims costs in those areas. This is likely due to the higher natural peril risk in northern Australia, particularly for flood and cyclone.

Technical premiums reduced on average across all regions due to the effect of premium adjustments and discounts applied by insurers. Regions with the highest technical premiums experienced the greatest premium adjustment reductions. The largest adjustment was in north Western Australia with a reduction of $324 to the technical premium on average, followed by north Queensland with $256.

As explained in Section 4.3, insurers apply adjustments for a variety of reasons, including concentration risk, market adjustments, price optimisation, and capping or cupping. To some degree, these premium adjustment reductions may be indicative of 'capping'; which is where insurers limit price increases in any given year in order to minimise price shock for consumers at renewal. However, adjustments are usually temporary and these price increases to the technical premium will likely flow through to the retail premium at subsequent renewals. Trends which are placing upward pressure on the price of insurance, such as inflation and increased reinsurance costs, are discussed in detail in Section 2.3.

The taxes and duties applied to strata insurance premiums across Australia are the same as those for home insurance (see Section 7.2.1). A flat rate of 10% GST is applied to all general insurance products across Australia. The stamp duty applied varies from 9% to 11% across all jurisdictions except the ACT, which does not collect stamp duty on insurance. These are not a cost to the insurer; they are an added cost incurred by the consumer. Both are proportional to the premium, so the amount paid is higher in areas where premiums are higher. For example, north Western Australia had the highest average technical premium, and the highest average taxes and duties of $543. The rest of Australia had the lowest average taxes and duties of $306, due to having the lowest average technical premium.

As stamp duties are applied on the GST-inclusive amount of a premium, the effect of these duties is magnified. As premiums grow in northern Australia, so too does the dollar value of the amount paid in GST and stamp duty (which is levied on the GST-inclusive premium amount).[305]

After taking into consideration adjustments to the technical premiums, we find that north Western Australia had the highest average retail premium of $3,128 for strata insurance up to a sum insured of $2 million, followed by north Queensland with $2,413, and the rest of Australia with $1,489.

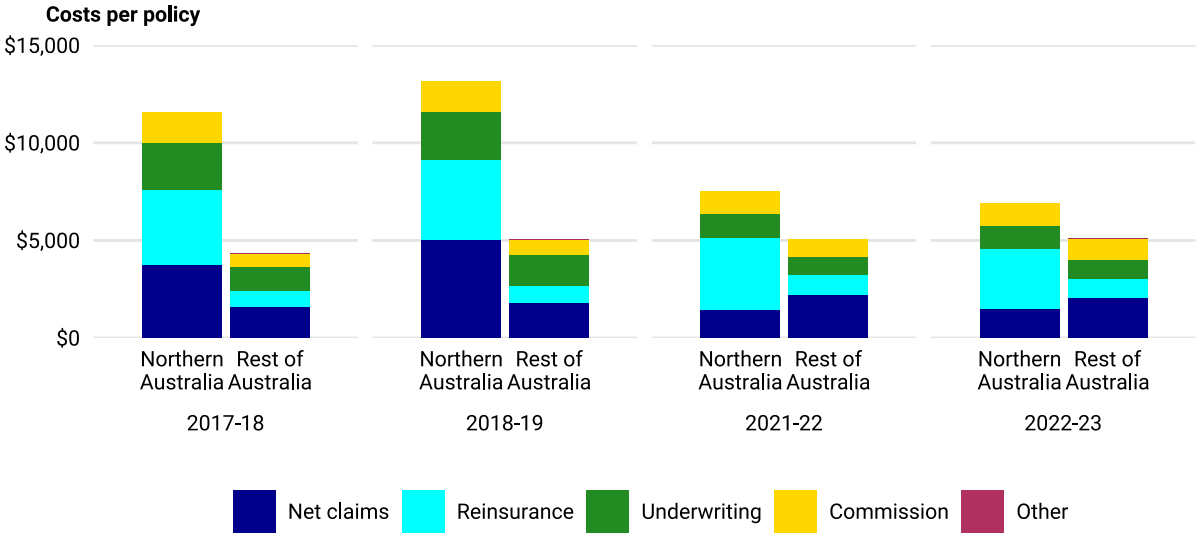
8.2.2 Insurer costs incurred

Similarly to home insurance, strata insurance has the same broad cost categories outlined in Section 7.2.2; net claims costs, reinsurance costs, underwriting costs and commission costs.

It should be noted that costs incurred are not directly used to calculate premiums. Instead, insurers use modelling to forecast costs they anticipate they will likely incur over the duration of the policy. As actual costs will not always align with forecasted costs, this can result in insurers over or under collecting sufficient premium to cover their expenses in any given year.

Figure 8.17 compares the average (inflation adjusted) cost incurred by cost category for strata policies for 2017–18, 2018–19, 2021–22, and 2022–23, for northern Australia compared to the rest of Australia. Over this period, the average cost per policy in the rest of Australia has been rising steadily (from $4,317 in 2017–18 to $5,128 in 2022–23), driven by increases in commission, reinsurance, and net claims costs. Underwriting costs have decreased over this time in both the rest of Australia (by $260) and northern Australia (by $1,233). Average costs in northern Australia have been considerably lower in the last 2 years ($7,546 in 2021–22 and $6,939 in 2022–23) compared to 2017–18 ($11,570) and 2018–19 ($13,150). Reinsurance and commission costs have decreased slightly in real terms. The overall decrease is largely due to a substantive decrease in average net claims cost (from $3,714 in 2017–18 to $1,476 in 2022–23) to levels below that of the rest of Australia ($2,017 in 2022–23). This is likely due to the low number of significant events impacting northern Australia over the past 2 years compared to the rest of Australia.

Figure 8.17: Average cost incurred per policy by cost categories for strata insurance, by region, 2017–18 to 2022–23, adjusted for inflation



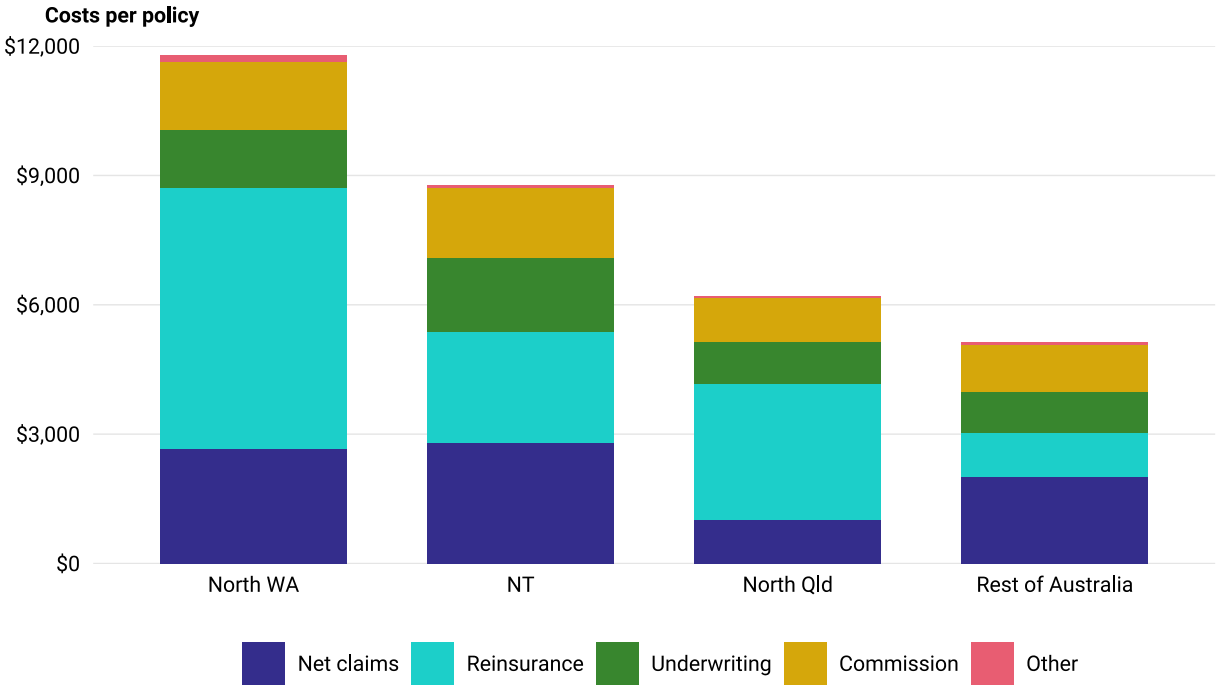
Source: ACCC analysis of data obtained from insurers.

305 ACCC, *NAII final report*, p 54.

Figure 8.18 below shows the average allocation of costs incurred per policy for strata insurance in 2022–23. Policies in north Western Australia cost insurers an average of $11,788 per policy in 2022–23, followed by Northern Territory with $8,761. These 2 regions had very similar net claims, underwriting, and commission costs. However, the difference was the large reinsurance cost in north Western Australia of $6,045 compared to $2,571 in the Northern Territory. North Queensland had the lowest net claims per policy at just $1,018, but the total costs were still higher than the rest of Australia due to having the second highest reinsurance cost at $3,151. The rest of Australia had the lowest average cost per policy of $5,128, largely because it had the lowest reinsurance cost of just $1,023, which is more than $1,500 less than all other regions.

Commission cost was much larger in north Western Australia and the Northern Territory, at $1,584 and $1,611 per policy, compared to $1,072 and $1,036 per policy in the rest of Australia and north Queensland. Commission expense can be high for strata insurance due to the heavily intermediated nature of strata insurance markets.

Figure 8.18: Average cost incurred per policy by cost categories for strata insurance, by region, 2022–23



Source: ACCC analysis of data obtained from insurers.

There are 2 main types of consumer intermediary in the supply of residential strata insurance products; insurance brokers and strata managers. Bodies corporate (often via a strata manager) will generally need to engage an insurance broker to access residential strata insurance products from insurer intermediaries. This is due in large part to the complexity of assessing and underwriting large strata properties. Insurance brokers will have a specialised understanding of the insurance arrangements required to ensure a strata property is adequately insured. As such, the vast majority of residential strata insurance products are distributed via insurance brokers.[306]

Commissions tend to be a percentage of the base premium, and are paid to the insurance broker by the insurer or insurer intermediary they place the insurance policy with. As residential strata insurance product premiums are generally much higher than home and contents insurance products, insurance brokers tend to earn a much larger commission from residential strata products than from home and contents products.

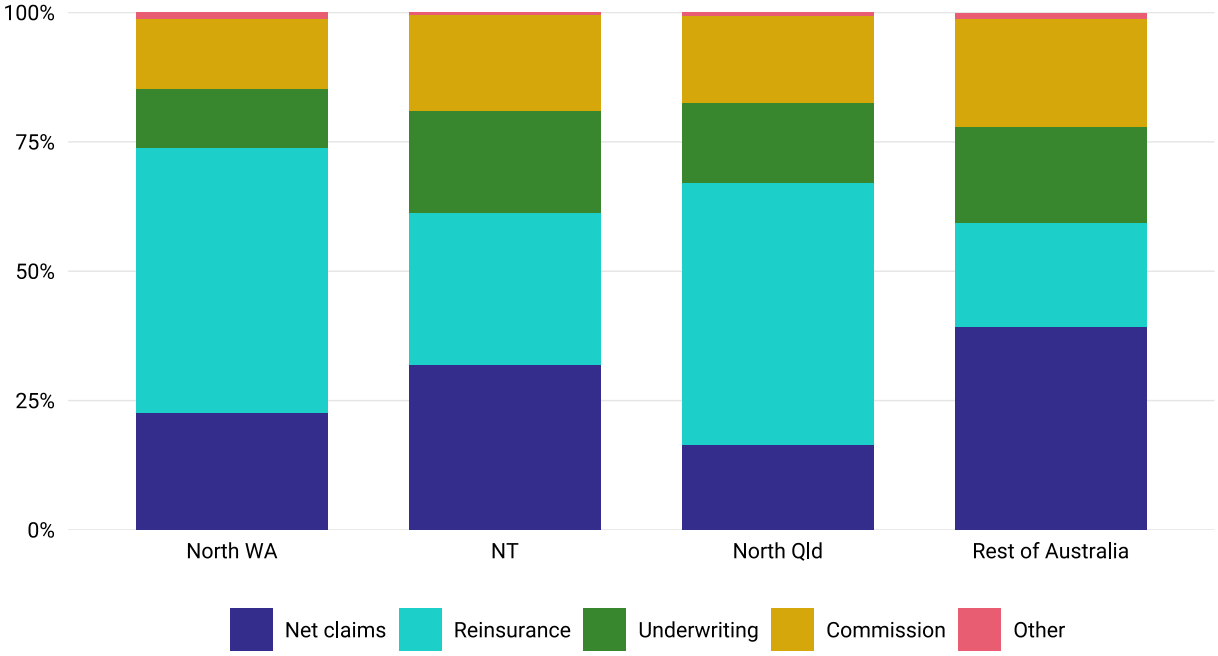
306 ACCC, *NAII final report*, p 393.

Commissions that are calculated as a percentage of the base premium result in properties with a higher exposure to risk paying more for the services of an insurance broker than less risk-exposed properties. In this regard, commissions can have a compounding effect on affordability concerns. However, some brokers are moving to fee for service models for clients located in high-risk areas in order to reduce the retail premium.[307]

Figure 8.19 below shows the proportional breakdown of cost categories by region for strata insurance in 2022–23. Reinsurance made up 51% of total costs in north Queensland and north Western Australia. Net claims were the largest in the rest of Australia at 39%, but this was offset by the smallest reinsurance cost at 20%. Commission cost was the largest in the rest of Australia at 21%, due to claims and reinsurance costs being a lower combined proportion than in northern Australia.

Of the 3 northern Australian regions, insurers appeared to retain the most risk in the Northern Territory, with net claims making up 32% and reinsurance making up just 29%. This makes the Northern Territory the only northern Australian region where net claims were a larger expense than reinsurance.

Figure 8.19: Proportions of cost categories for strata insurance, by region, 2022–23



Source: ACCC analysis of data obtained from insurers.

307 ACCC, *NAII final report*, p 394.

Reinsurance cost

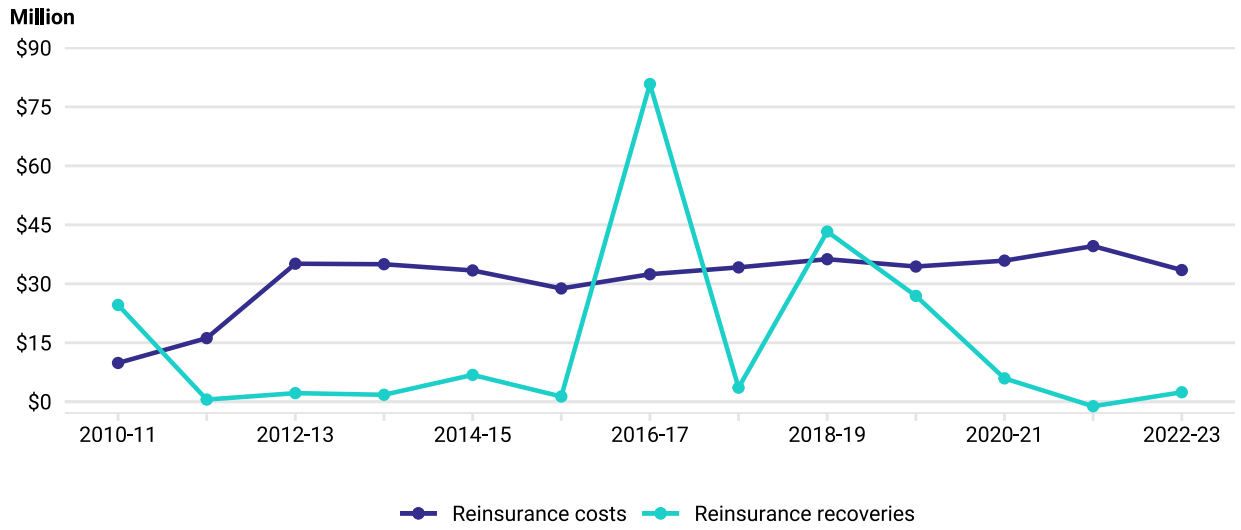
Insurers purchase reinsurance to protect themselves against large losses from catastrophic events. Reinsurance costs are the largest cost to insurers after net claim costs. In calculating the technical premium, insurers take into account the net cost of reinsurance, that is the reinsurance premium less expected reinsurance recoveries from the reinsurers.

Figure 8.20 shows inflation adjusted reinsurance costs and recoveries from 2010–11 to 2022–23, for strata insurance policies written in northern Australia. For the insurers in our sample, reinsurance costs peaked at $40 million in 2021–22 and then fell to $33 million in 2022–23. Reinsurance recoveries were at their highest in 2016–17 at $81 million, followed by $43 million in 2018–19, and have been less than $6 million since 2020–21. The spikes in reinsurance recoveries in 2010–11, 2016–17 and 2018–19 were due to Cyclone Yasi, Cyclone Debbie, and the Townsville floods, which caused reinsurance recoveries to exceed reinsurance expenses in northern Australia.[308] Recoveries did not exceed reinsurance costs in the last 4 years. This may be because insurers have continued to incur reinsurance costs but have had minimal recoveries due to limited significant events during this period. When interpreting this trend, it should be noted that insurers may not necessarily be purchasing the same level or type of cover each year. If insurers choose to retain more risk, this may result in lower reinsurance costs if rates are comparable to previous years.

As few insurers were in the pool at the time this data was collected (30 June 2023), we do not expect that the impact of the pool on reinsurance costs is evident at this time.

We note that the reinsurance recovery amount has been calculated on an incurred basis, taking into account claims paid and movement in reserves. This can result in negative reinsurance recoveries such as in 2021–22. Negative reinsurance recovery indicates reduction in reinsurance recovery on an incurred basis, possibly due to corrections related to the previous year.

Figure 8.20: Reinsurance costs and recoveries for strata insurance, northern Australia, 2010–11 to 2022–23, adjusted for inflation



Source: ACCC analysis of data obtained from insurers.

308 ACCC, *NAII final report*, p 101.

Similarly to Chapter 7, we looked at cession ratios across insurers that provide strata insurance. The cession ratio is the reinsurance expense divided by gross earned premium. It gives an indication of how much risk insurers retain or pass on to reinsurers. The higher the cession ratio, the higher the risk passed on by the insurer to the reinsurer and vice versa. Due to data limitations and the limited size of the strata insurance market, we are unable to graphically present the results. However, we note that there is a wide range in the cession ratios across insurers. Unlike home and contents insurance, some insurers had very high cession ratios, indicating that they are participating in the market by passing most of the risk on to reinsurers.

Consistent with home and contents insurance, reinsurance cost for strata is typically higher in northern Australia than in the rest of Australia. A large proportion of this is due to cyclone risk. In north Queensland for example, insurers spent an average of $527 per policy on reinsurance for cyclone for strata policies with a sum insured of less than $2 million. This is compared to just $56 for the rest of Australia. This is the largest reinsurance cost component for north Queensland, making up 74% of the $715 average reinsurance expense per policy, compared to 24% of the $239 in the rest of Australia. Unfortunately, due to data limitations we are unable to publish the average cyclone reinsurance cost component for strata properties in the Northern Territory or north Western Australia, or those with a sum insured of over $2 million.

9. Small business insurance

Small to medium enterprises (SME) will often seek insurance to protect against financial loss caused by damage to properties, protect assets and manage other commercial risk exposures such as professional indemnity and public liability. The types of coverage needed may depend on the type of business and the products or services it provides. There are some types of insurance for businesses that may be compulsory for business operations, such as employee compensation, public liability, product liability and professional liability. However, whether a business chooses to purchase insurance to protect against losses to property and business interruption may be more a decision based on the businesses' perception of risk and affordability of cover.[309]

In this chapter, we focus on SME insurance (building and contents) and business interruption insurance to the extent these are covered by the pool. Section 9.1 outlines in detail the scope of the pool's coverage as it relates to SME insurance.

In Section 9.2, we examine the average premium paid for SME insurance and illustrate the regional differences in price. Similar to the findings in Chapters 7 and 8, we find that prices are higher in northern Australia, even when controlling for differences in excess and the sum insured.

In Section 9.3, we outline the breakdown of retail premiums for SME insurance into the various cost components that contribute to the premiums charged to the policyholder. We also discuss the extent to which insurers choose to cede their risk to reinsurers.

The figures presented in this chapter show information up until 30 June 2023. As only a few insurers had joined the pool at the time, our analysis of the pool's effect is necessarily limited, particularly on SME observations. That is, of the insurers who had joined the pool before 30 June 2023, Sure does not write business policies, and Allianz only transferred household policies into the pool initially (see Chapter 3). We expect to begin to observe the impact of the pool on SME insurance in future reports once a greater number of insurers have been in the pool for a longer period.

Unlike Chapters 7 and 8 on home and strata insurance, respectively, SME insurance was not within the terms of reference for the Northern Australia Insurance Inquiry.[310] For this reason, information for years prior to the commencement of our monitoring role is limited in this chapter. Over the course of our monitoring role, we intend to build on the information that we have collected to provide a long-term view of SME insurance.

9.1 SME insurance policies eligible under the pool

As discussed in Chapter 1, the pool covers SME policies with a maximum of $5 million total sum insured across all eligible risks covered by the pool; these being building, contents, and business interruption.[311] Business interruption cover, in this context, refers to losses a business may suffer from being unable to trade for a period due to cyclone or cyclone-related flood damage. While all businesses are vulnerable to the impacts of cyclones, the pool does not cover businesses with a sum insured value above $5 million. Under our monitoring direction, we do not collect and analyse prices of SME policies with a sum insured above $5 million, so where we make a general reference in this chapter to SME insurance, we mean policies with a sum insured less than $5 million.

309 Small Business Commissioner, *Small business insurance: contemporary challenges and experiences*, August 2022, accessed 21 September 2023, p 14.

310 Aside from a case study on the 2019 Townsville floods, analysis of commercial (property, contents, and business interruption) insurance was outside the scope of the Northern Australia Insurance Inquiry.

311 ARPC, *Reinsurance Pools, Cyclone*, ARPC website n.d, accessed 8 August 2023.

Provided such losses are covered under a business's insurance policy, the types of losses eligible for pool coverage include the direct and indirect costs of restoring the physical aspects of the property, including debris removal and repairs. Consequential loss arising from damage to property (e.g. temporary accommodation costs; loss of rental and business income) is also covered by the pool.[312]

Insurance policies providing building and contents cover for a hotel, motel, boarding house, or aged care facility (as examples of SME) are eligible policies, subject to the maximum sum insured test. Charities and not-for-profit property policies are generally subject to the test as well, but any property used for residential purposes (e.g. community housing) does not count towards the maximum sum insured in the SME insurance policy.

In the event a SME policy covers both residential and non-residential buildings or contents, only the non-residential coverage counts towards the maximum sum insured test. If the non-residential component exceeds the test's threshold, then the entire policy (including the residential part) is not eligible. In this circumstance, the residential building and/or contents must be insured separately from the non-residential aspect to be eligible under the pool.[313]

Where we have represented and commented on premium distributions in this chapter, there is often a large spread of median prices between insurers. This is likely due to insurers having different risk appetites and a preference to target specific, disparate industries and professions, from very small enterprises up to the maximum $5 million sum insured limit (see Section 6.2.3).

9.2 Prices of SME insurance

This section provides information on SME insurance prices for policies with a total sum insured of up to $5 million. Similar to Chapters 7 and 8, we look at SME insurance prices in several ways: premiums and the range of premiums (Section 9.2.1), premiums per $100,000 sum insured (Section 9.2.2), premiums by excess (Section 9.2.3), and average premiums by sum insured and excess (Section 9.2.4).

In addition to providing average values, we have also included box plots showing the range of premiums, where appropriate.[314] This allows for a deeper look at the prices paid by a wider range of SME policyholders. This is particularly important when looking at outcomes for consumers, as there can be wide variations in average annual premiums for SME policies, depending on the type and size of business insured.

9.2.1 Premiums for SME insurance

This section provides information on premiums paid for SME insurance policies with a total sum insured of less than $5 million. For comparability purposes with earlier chapters, we have chosen to focus mainly on SME combined building and contents policies. The average premiums presented are the mean value of the premiums for SME products supplied by insurers at a postcode or regional level. They include GST, stamp duty and applicable levies, and are presented in real terms (in 2022–23 dollars). The reported premiums do not include additional fees that may be applied by an insurance broker for arranging insurance. Quoted premiums which were not ultimately taken up by consumers were also not included.

Figure 9.1 below shows that compared to the previous year, average premiums for SME combined building and contents insurance (for policies with less than $5 million total sum insured) increased

312 Explanatory Memorandum [1.55], p 12. Note: not all risks covered by the pool will be covered by every individual SME policy.

313 Explanatory Memorandum [1.73], p 15.

314 See Chapter 7 for further explanation on what these charts illustrate.

across the country, after adjusting for inflation. Premium increases between 2021–22 and 2022–23 were, on average, higher for north Western Australia and the Northern Territory than the other regions. North Western Australia saw an average premium increase of 14%, raising the average premium to $6,287. Similarly, the Northern Territory premiums rose on average 13% to $3,670, while north Queensland and the rest of Australia both increased on average 7% to $3,095 and $1,930, respectively. In nominal terms, these increases were 22%, 21%, 15% and 15% for north Western Australia, the Northern Territory, north Queensland and the rest of Australia, respectively.

Figure 9.1: Average premium for SME combined building and contents insurance, by region, 2021–22 to 2022–23, adjusted for inflation

Source: ACCC analysis of data obtained from insurers.

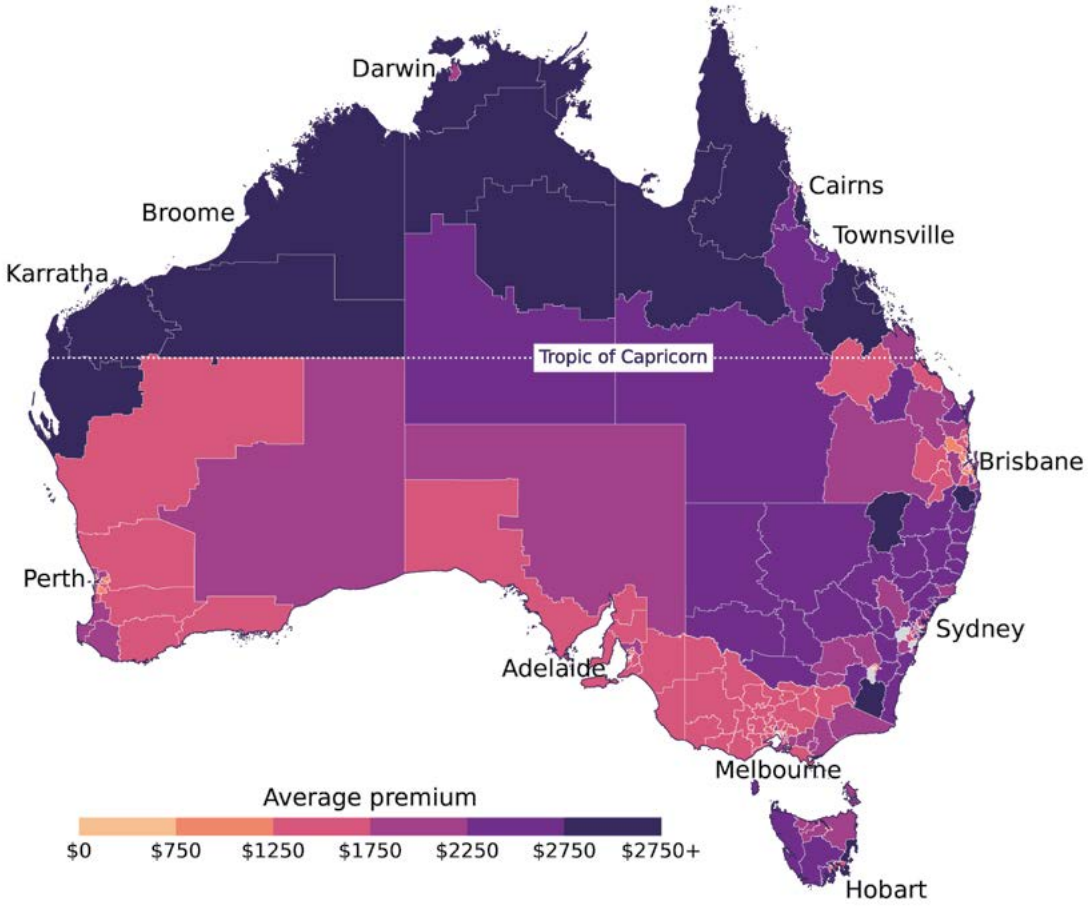
Similar to trends in the figure above, Figure 9.2 below shows that, compared to the previous year, average SME business interruption premiums increased across all regions in real terms, for policies with less than $5 million total sum insured. North Western Australia experienced the largest increase on average of 22% to $1,781, followed by north Queensland with a 21% increase to $1,141. The Northern Territory had the smallest increase of 2% to $1,210, although the rest of Australia still had the lowest average premiums at $760.

Figure 9.2: Average premium for SME business interruption insurance, by region, 2021–22 to 2022–23, adjusted for inflation

Source: ACCC analysis of data obtained from insurers.

Figure 9.3 below shows that northern Australian regions had the highest average premiums for SME combined building and contents insurance. Some higher cost areas can also be seen through parts of New South Wales.

Figure 9.3. Average premium for SME combined building and contents insurance, by Statistical Area Level 3, in 2022

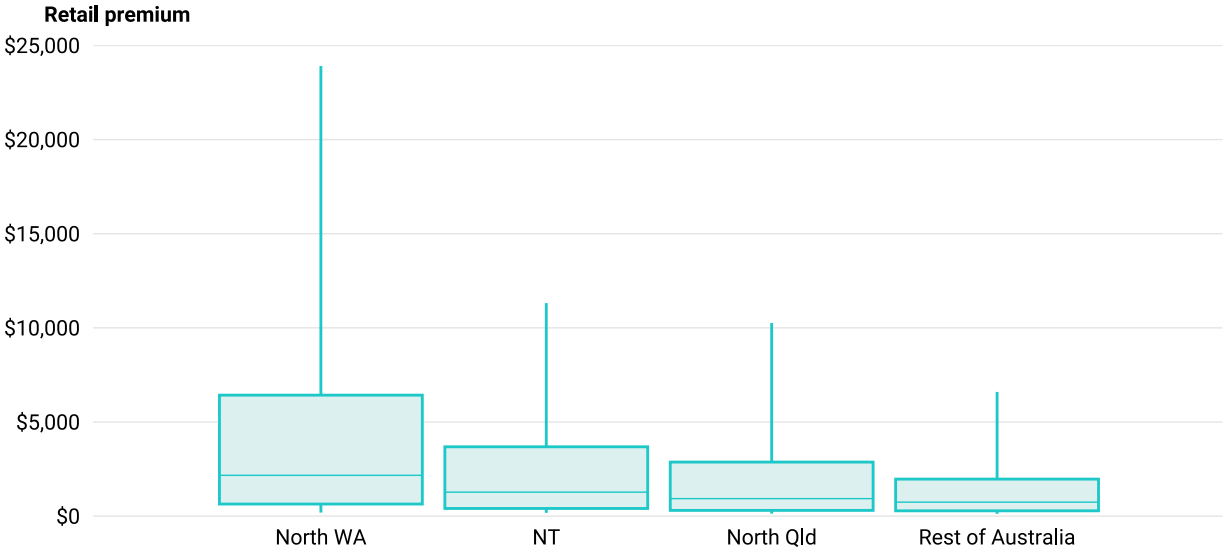


Source: ACCC analysis of data obtained from insurers.

As seen in Figure 9.4 below, north Western Australia had the highest median premium for SME combined building and contents insurance, for policies with less than $5 million total sum insured. For SME combined building and contents insurance, the median premium in north Western Australia was $2,168. This is almost 3 times as high as the rest of Australia, which had the lowest median premium at $743. Median premiums for the Northern Territory and north Queensland were $1,275 and $930, respectively. North Western Australia also shows a greater range of premiums than other regions. In northern Australia, 35% of SME policyholders, in our sample, paid more than $2,000 for combined building and contents insurance, compared to 25% for the rest of Australia. There appears to be less variation in median premiums between regions for SME combined building and contents insurance products compared to residential or strata products.

For policies in regions with medium to high risk of cyclone in northern Australia, the median premiums tended to be higher. For example, the median price for a SME combined building and contents policy in a location at medium to high cyclone risk was $6,259 in north Western Australia, and for north Queensland and the Northern Territory the medians were $4,818 and $4,440, respectively.

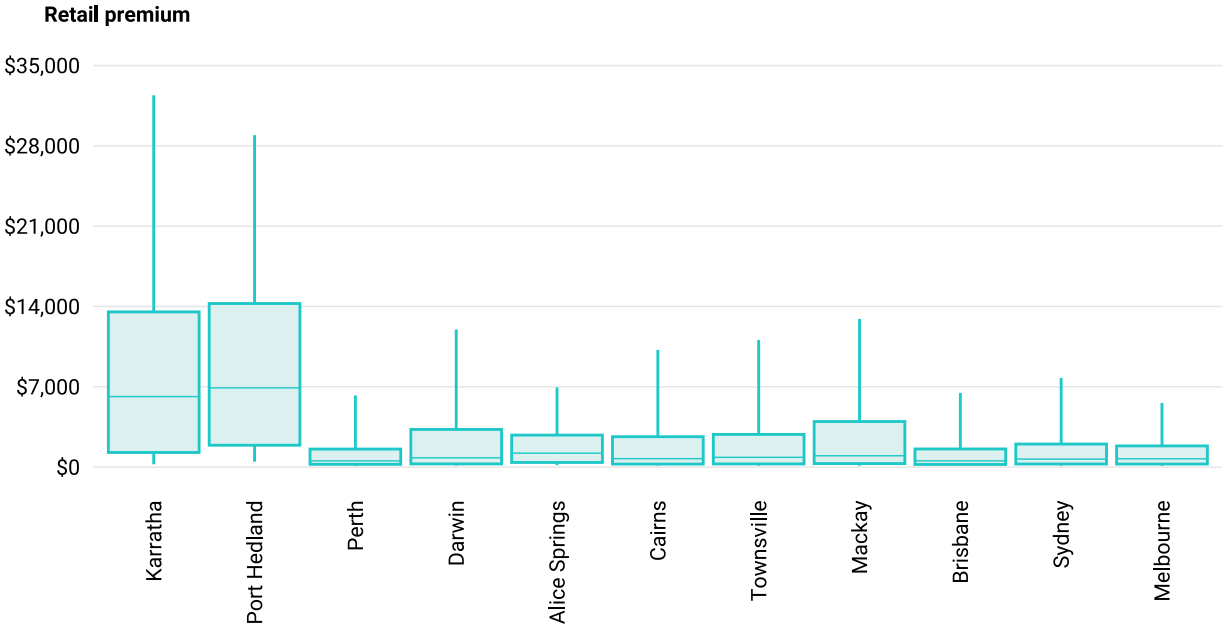
Figure 9.4: Distribution of retail premiums for SME combined building and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 9.5 below shows the distribution of SME combined building and contents premiums in select cities and towns for policies with a total sum insured of up to $5 million. The highest median premiums were seen in the north Western Australian cities of Port Hedland ($6,910) and Karratha ($6,147), followed by Alice Springs ($1,218), Mackay ($993), Townsville ($855) and Darwin ($812).

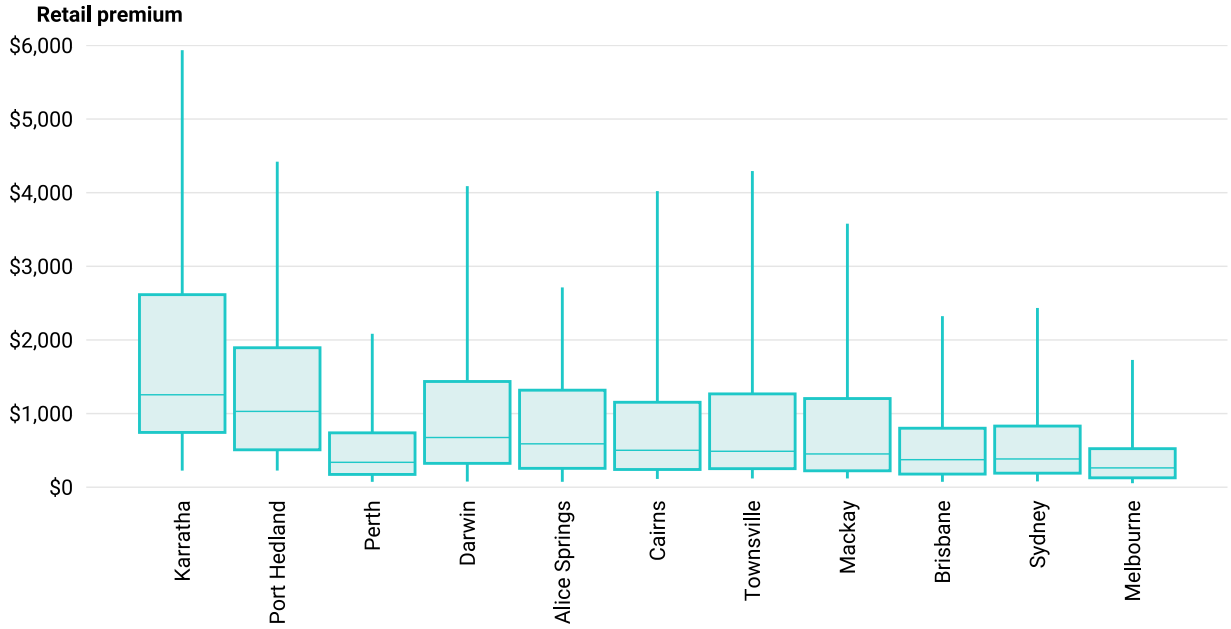
Figure 9.5: Distribution of retail premiums for SME combined building and contents insurance, select cities and towns, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 9.6 below shows the distribution of SME business interruption premiums for sums insured of up to $5 million, in select cities. Similar to Figure 9.5, it shows that highest median premiums were seen in the northern cities of Karratha ($1,255), Port Hedland ($1,030) and Darwin ($675), compared to southern cities like Sydney, Melbourne and Perth where the medians ranged between $262 and $384. The cities in northern Australia also tended to have a large spread of prices.

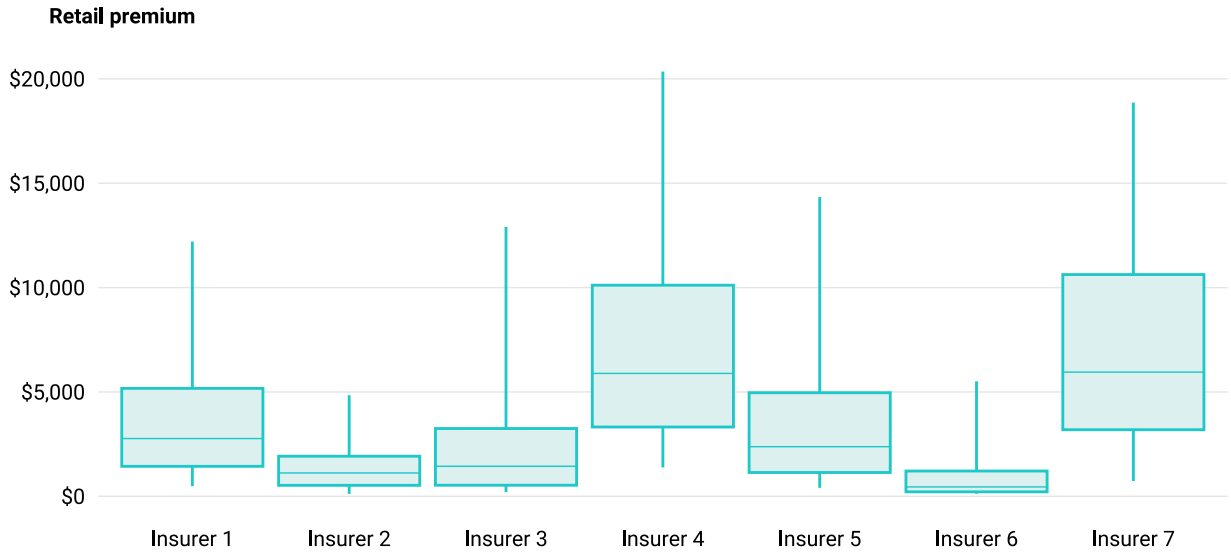
Figure 9.6: Distribution of retail premiums for SME business interruption insurance, select cities and towns, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 9.7 below shows the distribution of SME combined building and contents (up to $5 million sum insured) premiums in northern Australia by insurer. The median prices ranged from $452 (Insurer 6) to $5,952 (Insurer 7), with most insurers showing a wide range of premiums. The large spread of median prices between insurers is likely due to different risk appetites and targeting of specific, disparate industries and professions (Section 6.2.3).

Figure 9.7: Distribution of retail premiums for SME combined building and contents insurance, by insurer, northern Australia, 2022



Source: ACCC analysis of data obtained from insurers.

9.2.2 Premiums by sum insured

This section presents analysis on SME combined building and contents premiums per $100,000 sum insured for policies of up to $5 million sum insured (see Section 7.1.2. for a detailed explanation on the impact sums insured have on premiums).

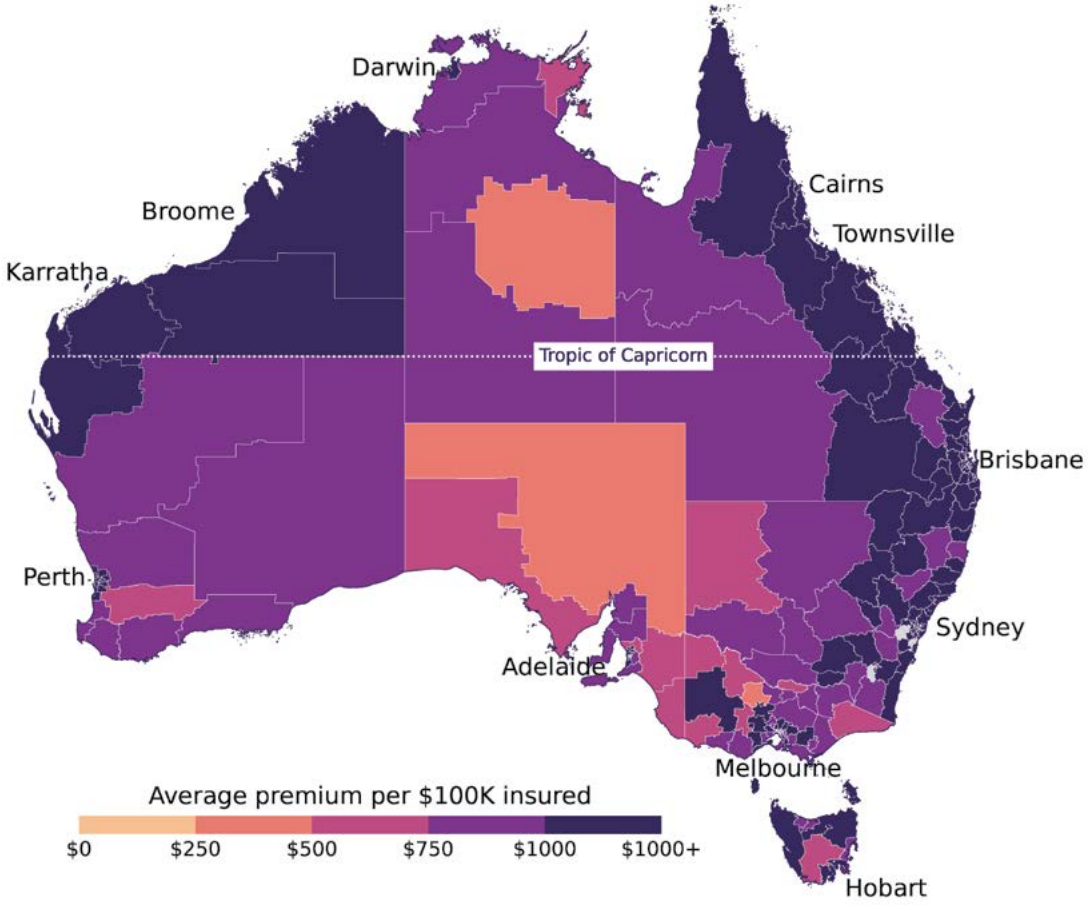
Figure 9.8 below shows that compared to 2021–22 average premiums per $100,000 sum insured for SME combined building and contents were higher across all regions in 2022–23. North Western Australia experienced a 16% increase and had the highest average across all regions ($943). The rest of Australia experienced a 4% increase and had an average of $412. North Queensland had an average of $630 and a 4% increase compared to the previous year, while the Northern Territory had an average of $502 and a 2% increase. These increases, apart from north Western Australia, are not of the same magnitude as the average premiums increases presented in Figure 9.1. It may be the case that the value of sums insured has also increased, but at a higher rate than premium increases. This may be a reflection of insurers offering higher sums insured to address the effects of inflation and rising construction costs (which are discussed in Section 2.3).

Figure 9.8: Average premium per $100,000 sum insured for SME combined building and contents insurance, by region, 2021–22 to 2022–23

Source: ACCC analysis of data obtained from insurers.

Figure 9.9 below shows the average premium per $100,000 sum insured for SME combined building and contents policies across Australia with a total sum insured up to $5 million. As can be seen by the darker (purple) coloured shading, many northern regions were found to be paying higher prices per $100,000 sum insured than southern Australia. All of north Western Australia was seen to be paying more than $1,000 per $100,000 sum insured on average, as with many north Queensland regions.

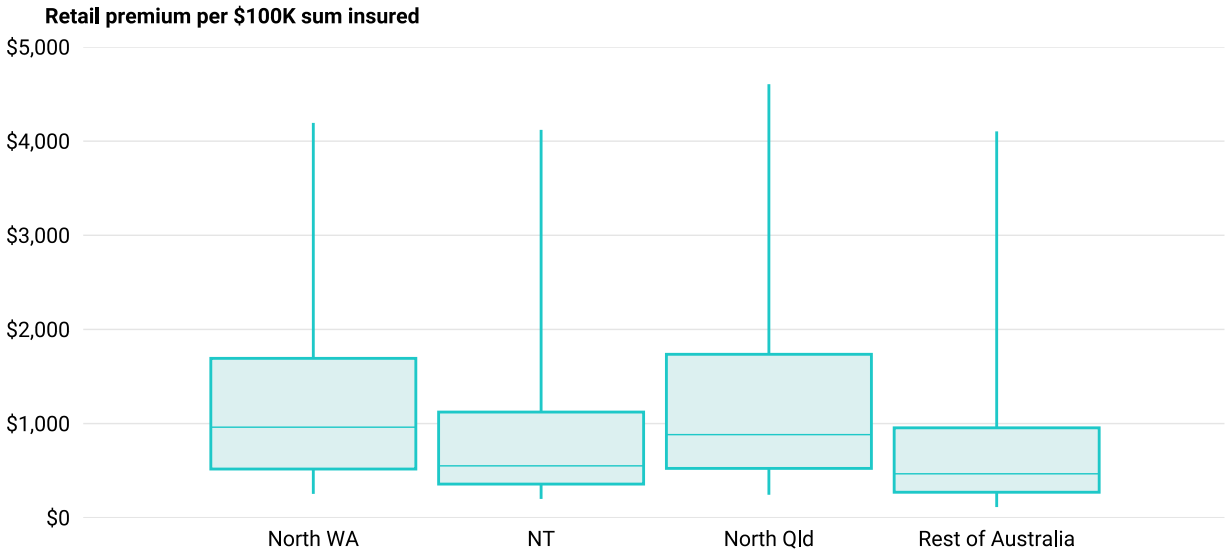
Figure 9.9: Average premium per $100,000 sum insured for SME combined building and contents insurance, by Statistical Area Level 3, in 2022



Source: ACCC analysis of data obtained from insurers.

Figure 9.10 shows the distribution of premiums per $100,000 sum insured for SME combined building and contents policies up to $5 million sum insured. North Western Australia had the highest median of $962, followed by north Queensland at $883. The medians for the Northern Territory ($551) and the rest of Australia ($467) were much lower. North Western Australia and north Queensland also had the largest spread of prices. A reason for this spread may be due to the large variety and types of SME businesses, with different levels of risk and different levels of coverage.

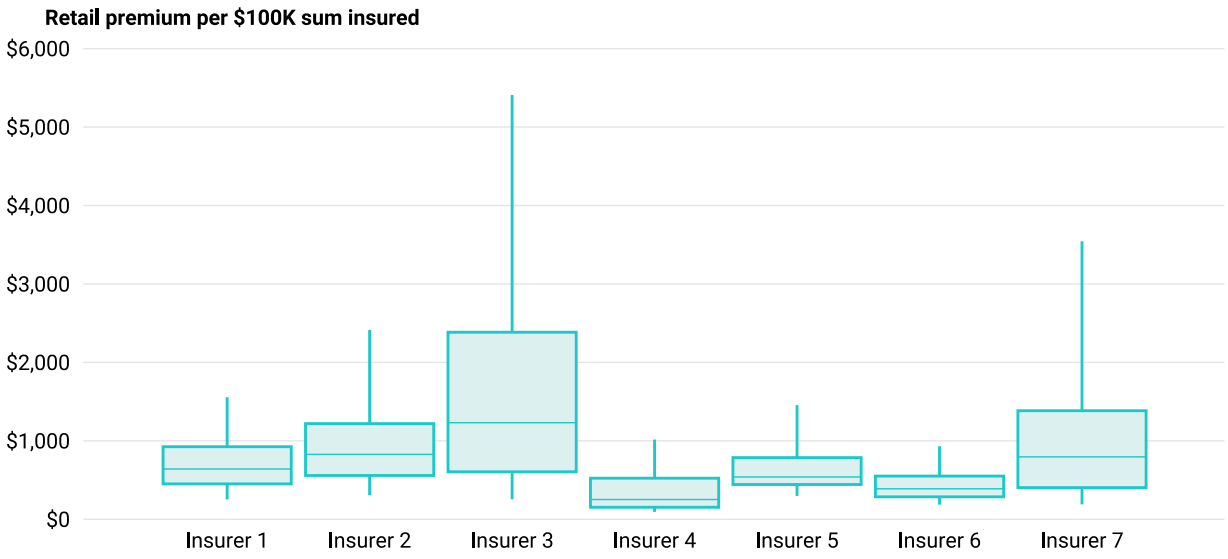
Figure 9.10: Distribution of retail premiums per $100,000 sum insured for SME combined building and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 9.11 shows a high degree of variability in the prices for SME policies per $100,000 sum insured sold by different insurers. Insurers 3 and 7 recorded the largest spread, with 90% of policies falling between $256 to $5,408, and $191 to $3,544 respectively. Insurer 3 also had the highest median by sum insured ($1,232) while Insurer 4 had the lowest median by sum insured ($253).

Figure 9.11: Distribution of retail premiums per $100,000 sum insured for SME combined building and contents insurance, by insurer, northern Australia, 2022



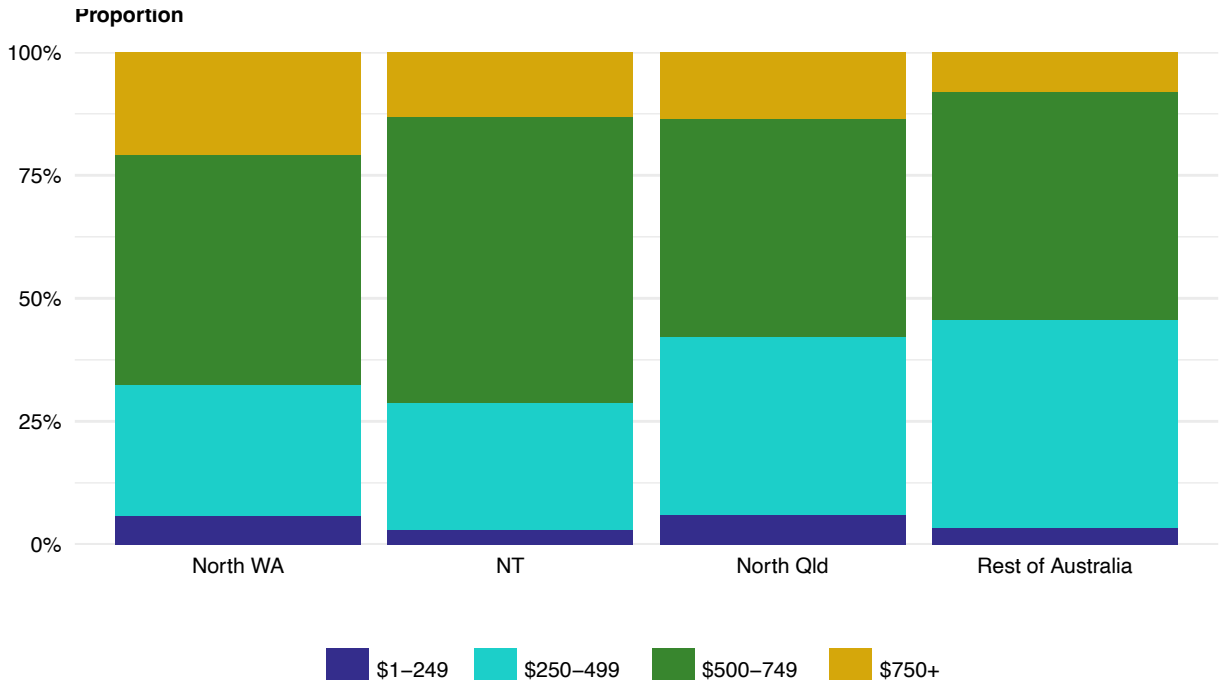
Source: ACCC analysis of data obtained from insurers.

9.2.3 Premiums by excess

This section presents an analysis of the excess levels selected by SME policyholders, and average premiums when the excess is held constant (see Section 7.1.3 for a detailed explanation on the relationship between excesses and premiums, which also applies here).

Figure 9.12 below shows that excess levels in northern Australia were on average higher than in the rest of Australia for SME combined building and contents policies. Compared to residential and strata insurance, excesses showed less variability between regions for SME policies. The Northern Territory had the highest proportion of policies with an excess over $500, with 71%. This contrasts with our findings for strata and residential insurance, where the Northern Territory had the lowest or second lowest excess levels. North Western Australia had the highest proportion of policies with an excess over $750 (21%).

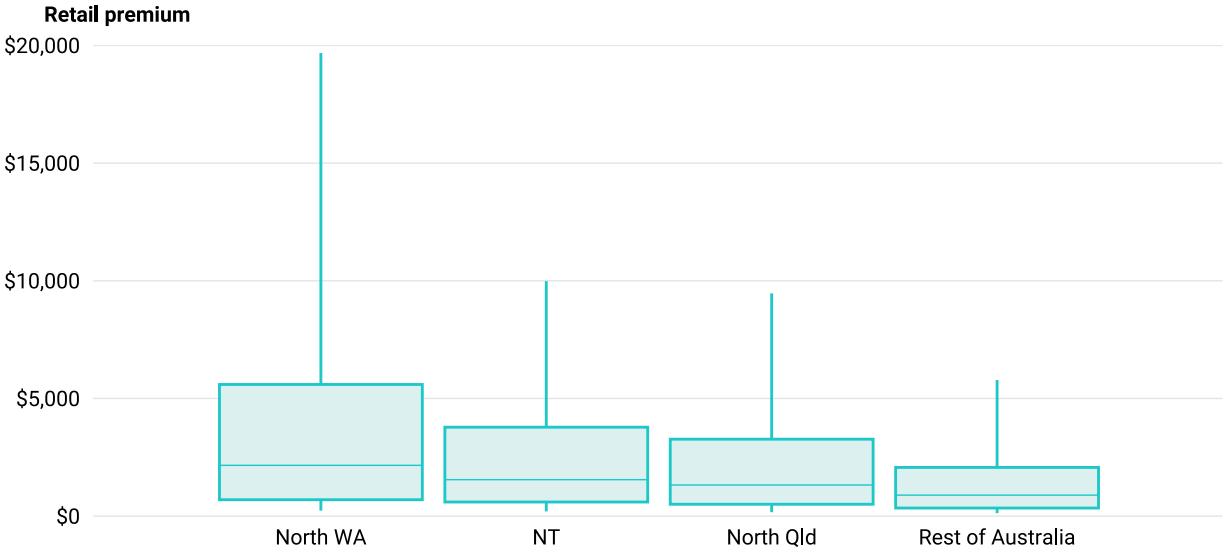
Figure 9.12: Proportions of excess brackets for SME combined building and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Figure 9.13 shows that north Western Australia had the highest median price ($2,158) across all regions for SME combined building and contents policies with policy excess amounts between $250 and $500. The Northern Territory had the second highest median ($1,550), closely followed by north Queensland with a median of $1,323. The rest of Australia had a median of $893.

Figure 9.13: Distribution of retail premiums for SME combined building and contents insurance, excess between $250 and $500, by region, 2022



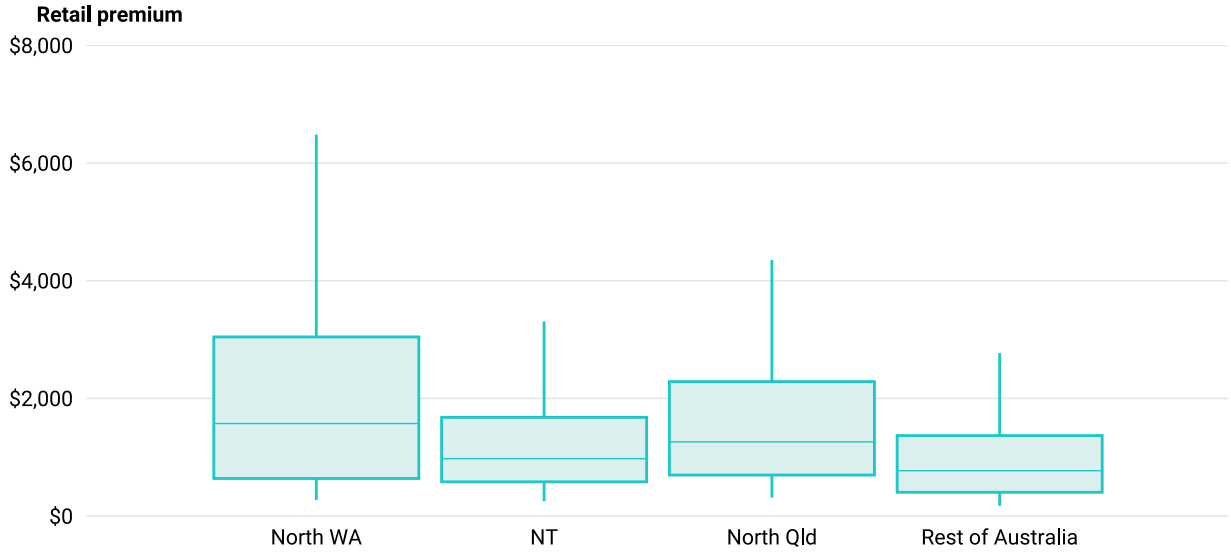
Source: ACCC analysis of data obtained from insurers.

9.2.4 Premiums by excess and sum insured

This section presents analysis on the median premiums paid by SME combined building and contents insurance policyholders within select sum insured and excess levels. We aim to compare average premium outcomes by insurer and between regions when 'typical' sum insured and excess levels are selected. It should be noted that the sum insured and excess bands selected are based on what is typical across all SME combined building and contents policies and that analysis is limited to policies of up to $5 million sum insured. However, these levels may not be the typical or most common sum insured or excess levels for a particular insurer or a particular region.

Figure 9.14 below shows the premium distribution for SME combined building and contents policies across regions for 'typical' excesses between $250 to $500 and sum insured values of $40,000 to $600,000. Consistent with the findings in Sections 7.1.4 and 8.1.4, north Western Australia had the highest median price of all regions ($1,574) even at these 'typical' levels. North Queensland was second highest with a median of $1,262, followed by the Northern Territory ($977) and the rest of Australia ($772). North Western Australia also had the largest spread in prices.

Figure 9.14: Distribution of retail premiums for SME combined building and contents insurance, excess between $250 and $500, sums insured between $40,000 and $600,000, by region, 2022



Source: ACCC analysis of data obtained from insurers.

9.3 Breakdown of insurance premiums

This section provides a breakdown of retail premiums and examines insurer costs for SME combined building and contents insurance in different regions across Australia. Business interruption insurance is not included in this section. It should be noted that analysis in this section is limited to policies with a total sum insured of up to $5 million (which are those covered by the pool). The breakdown of retail premiums for SME insurance products in northern Australia are examined in Section 9.3.1, while insurer costs are examined in Section 9.3.2.

9.3.1 Breakdown of retail premiums

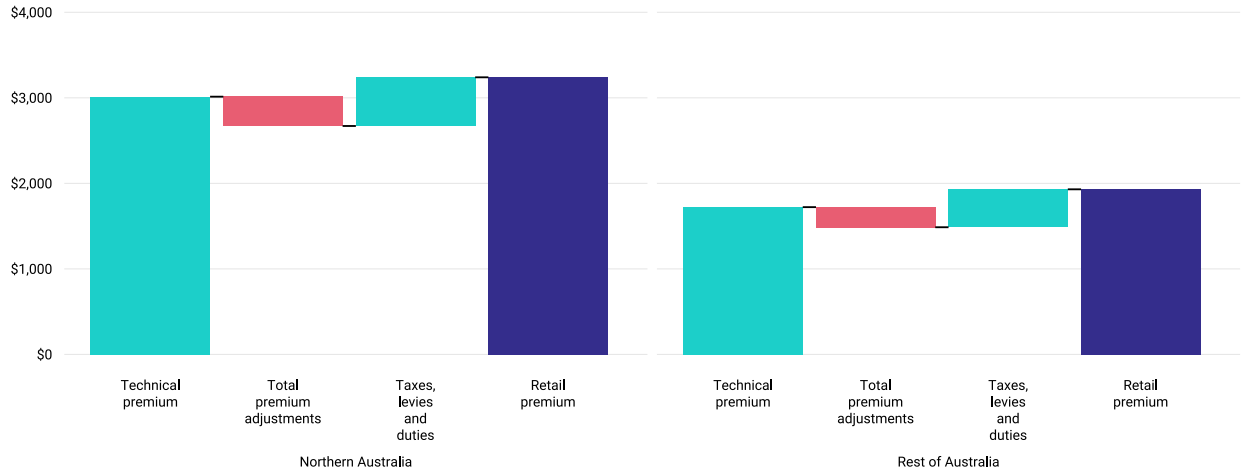
Similar to home and strata insurance, we have separated the average SME retail premiums into the technical premium, premium adjustments, and taxes, levies and duties as outlined in Chapter 7.

Figure 9.15 below shows the average result of each of these steps to calculating the retail premium for SME combined building and contents insurance in northern Australia compared to the rest of Australia as at September 2022. Unfortunately, due to data limitations we were unable to provide a breakdown of regions in northern Australia. We note that only records with complete (in other words, not missing) technical premiums, premium adjustments, taxes and levies, and retail premium values were included in the analysis. This means that the figures represent a large, but not complete, proportion of policies that we have obtained data for.[315]

Northern Australia had a high average technical premium at $3,014 compared to the rest of Australia with $1,722. The higher average technical premium in northern Australia is reflective of the higher claims and reinsurance costs. This may be due to the higher natural peril risk in northern Australia particularly for flood and cyclone, and possibly a different industry mix. SME businesses have a much more diverse risk profile than homes covered by general insurance.

315 Proportion of policies with complete data by region is as follows: Northern Australia (54%) and the rest of Australia (39%).

Figure 9.15: Average retail premium breakdown for SME combined building and contents insurance, by region, 2022



Source: ACCC analysis of data obtained from insurers.

Note: Only complete records containing technical premium, premium adjustments, taxes and levies and retail premium values have been included in this analysis.

Retail premiums were reduced on average across both regions due to premium adjustments and discounts applied by insurers. Northern Australia had a larger premium adjustment decrease, on average a reduction of $343 compared to the rest of Australia with $235.

As explained in Section 4.3, insurers apply adjustments for a variety of reasons, including concentration risk, market adjustments, price optimisation, and capping or cupping. To some degree, these negative adjustments may be indicative of 'capping'; which is where insurers limit price increases in any given year in order to minimise price shock for policyholders at renewal. However, adjustments are usually temporary and these price increases to the technical premium will likely flow through to the retail premium at subsequent renewals. Trends which are placing upward pressure on the price of insurance, such as inflation and increased reinsurance costs, are discussed in detail in Section 2.3.

Taxes and duties applying to general insurance include GST and state and territory stamp duties and, in some jurisdictions, other levies. The tax rates applied for home, strata, and SME insurance across Australia are provided in Table 7.1 in Chapter 7. These are not a cost to the insurer (or imposed by the insurer), but they are an added cost incurred by the policyholder. Both are proportional to the premium, so the amount paid is higher in areas where technical premiums are higher. For example, northern Australia had a high average technical premium, and a high average taxes and duties of $569. The rest of Australia paid a lower average amount of taxes and duties of $443 due to having a lower average technical premium.

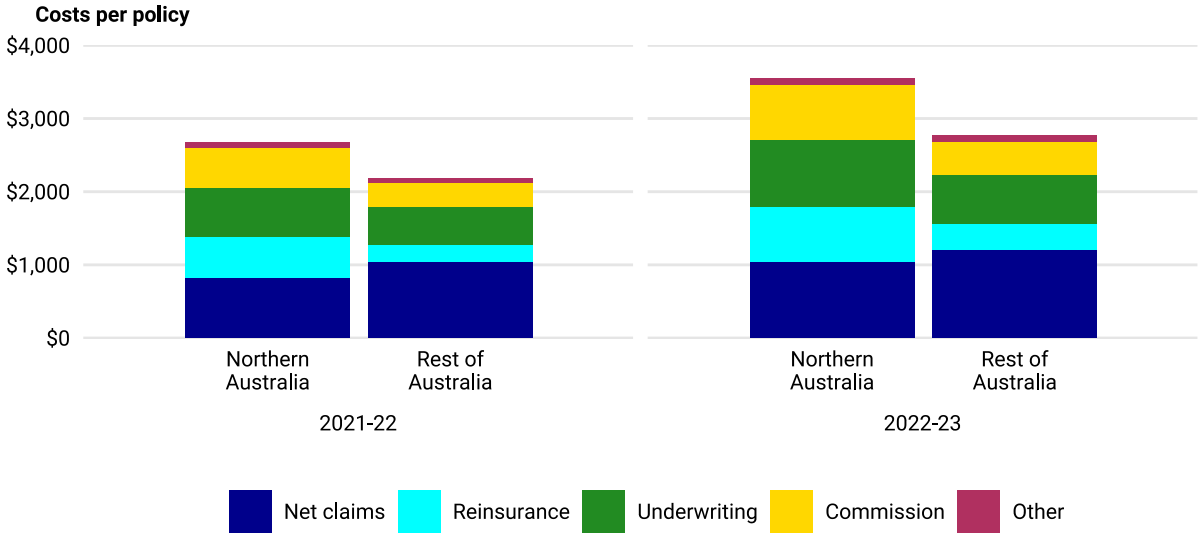
After taking into consideration adjustments to the technical premiums, northern Australia had an average retail premium of $3,240, compared to the rest of Australia with $1,930.

9.3.2 Insurer costs incurred

This section provides information on the costs incurred by insurers supplying SME combined building and contents insurance products. These costs can be divided into claims costs, reinsurance costs, underwriting costs and commission costs. Further detail about these costs is provided in Section 7.2.2. Our data collection and analysis includes SME combined building and contents policies with a maximum sum insured of $5 million.

Figure 9.16 below shows the average cost of various cost categories in northern Australia and the rest of Australia in 2021–22 and 2022–23. The average total costs incurred increased considerably across Australia from 2021–22 to 2022–23. Average costs in northern Australia increased from $2,678 to $3,551 per policy, and in the rest of Australia from $2,182 to $2,769 per policy. This increase was generally consistent across all cost categories, with the largest increases being net claims costs (up $218 in northern Australia) and underwriting costs (up $246 in northern Australia). Increases in reinsurance and commission costs were between $118 and $164 per policy in the rest of Australia and $194 to $210 per policy in northern Australia, respectively.

Figure 9.16: Average cost incurred per policy by cost categories for SME combined building and contents insurance, by region, 2021–22 to 2022–23, adjusted for inflation

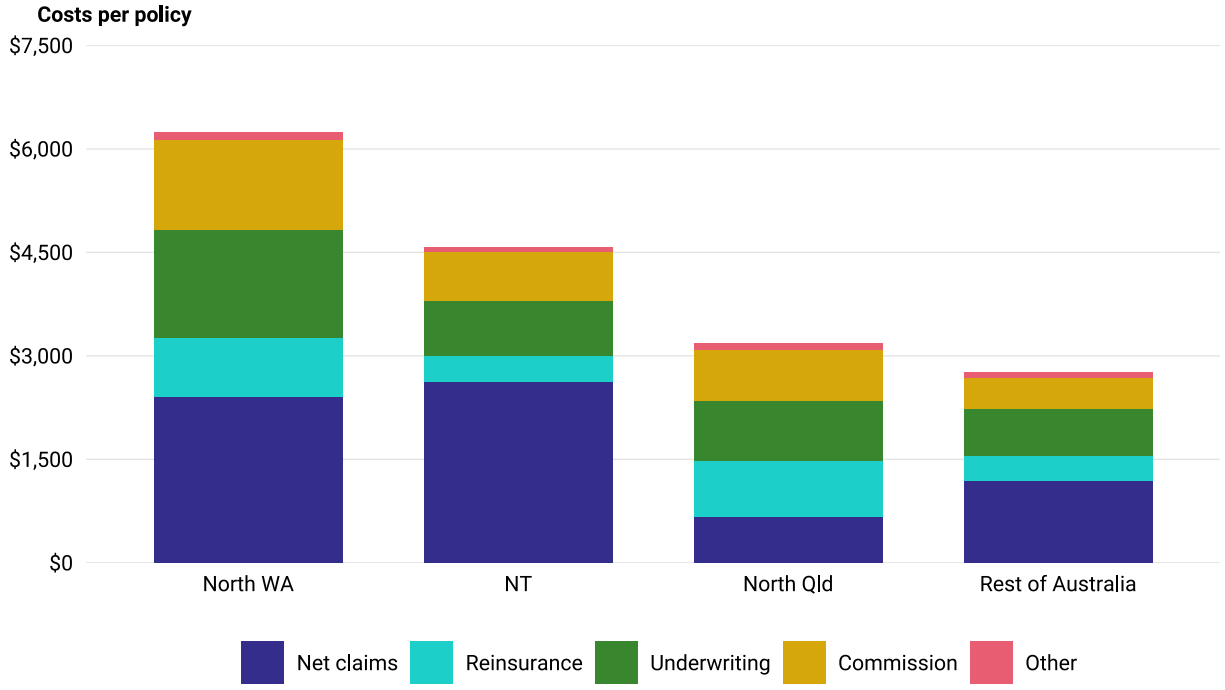


Source: ACCC analysis of data obtained from insurers.

Figure 9.17 below shows the average allocation of cost per SME combined building and contents insurance policy across northern Australia and the rest of Australia in 2022–23. North Western Australia had the highest average cost of $6,243 per policy, followed by the Northern Territory with $4,570, north Queensland with $3,182 and the rest of Australia with $2,769. The average cost in north Western Australia was over twice the rest of Australia. The main contributing costs in north Western Australia were net claims cost of $2,413, underwriting cost of $1,577 and commission cost of $1,305. Only the Northern Territory had higher net claims cost than north Western Australia, at $2,618 per policy.

Reinsurance costs per policy were on average highest in north Western Australia ($845) followed by north Queensland ($817). Commission costs on average were highest in north Western Australia ($1,305) compared to other regions. This was followed by $732 in north Queensland, $717 in Northern Territory and $450 in the rest of Australia. The higher commission cost in northern Australia compared to the rest of Australia is likely attributable to commissions usually being calculated as a percentage of premiums, and premiums being higher on average in northern Australia.

Figure 9.17: Average cost incurred per policy by cost categories for SME combined building and contents insurance, by region, 2022–23



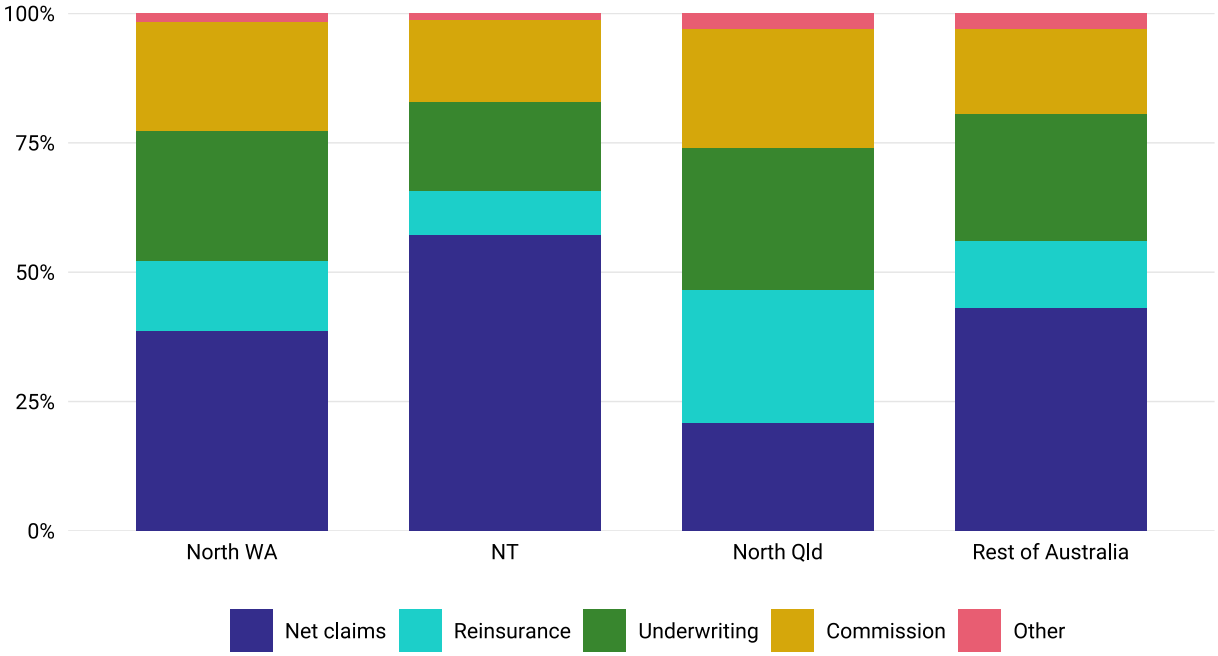
Source: ACCC analysis of data obtained from insurers.

Figure 9.18 below shows the proportional breakdown of cost categories by region for SME combined building and contents insurance in 2022–23. Net claims cost made up 57% of the total cost in the Northern Territory, the highest proportion of overall costs, compared with the rest of Australia (43%), and north Western Australia (39%). North Queensland had a very low proportion of net claims costs of just 21%. However, the proportion of reinsurance cost was highest in north Queensland at 26%, followed by north Western Australia and the rest of Australia, both around 13%. Reinsurance costs only made up around 9% of total costs in the Northern Territory.

While there are differences in how much risk insurers choose to cede to reinsurers, across regions, the combined net claims and reinsurance rate is relatively similar in north Western Australia, north Queensland, and the rest of Australia, between 46% and 56%. The Northern Territory was at 66% due to its high net claims rate. We will continue to monitor this in future years.

The contribution of underwriting costs ranged between 17% in the Northern Territory, and 24% to 27% in the other 3 regions. Commission costs were higher in north Queensland and north Western Australia, which is likely attributable to commissions usually being calculated as a percentage of premiums, and premiums being higher on average in northern Australia. Further monitoring reports will help to explain whether these observations hold over time or are specific to the year shown.

Figure 9.18: Proportions of cost categories for SME combined building and contents insurance, by region, 2022–23



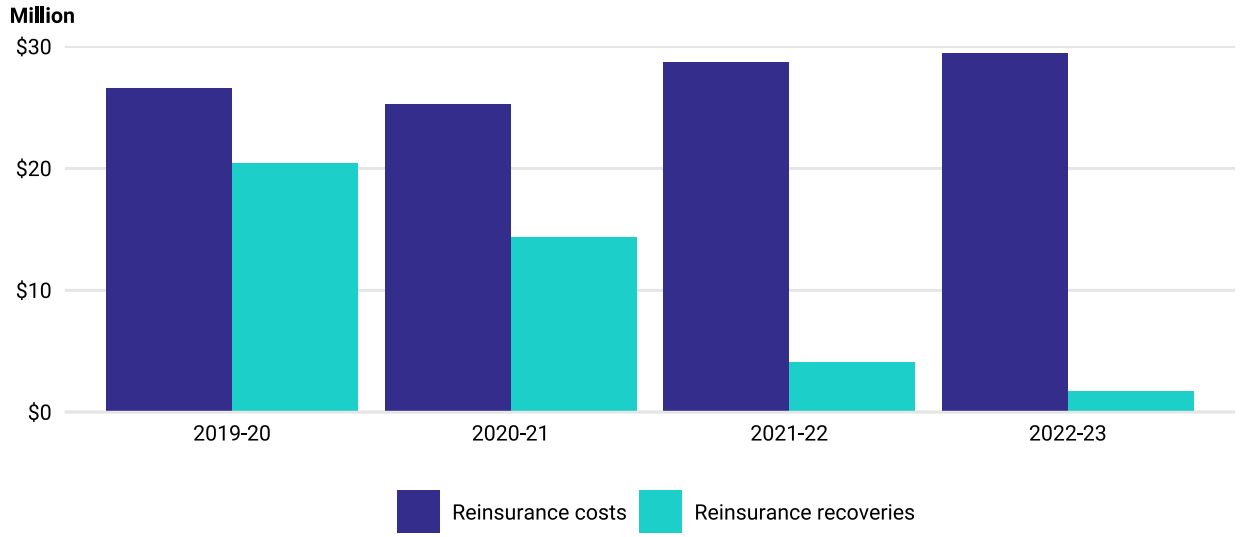
Source: ACCC analysis of data obtained from insurers.

Reinsurance cost

Insurers purchase reinsurance to protect themselves against large losses from catastrophic events. In calculating the technical premium, insurers take into account the net costs of reinsurance, that is the reinsurance premium less expected reinsurance recoveries from the reinsurers.

Figure 9.19 below shows reinsurance costs and recoveries from 2019–20 to 2022–23 for 9 insurers which we collected SME insurance information from. It should be noted that amounts are inflation adjusted for comparison purposes. Reinsurance costs in 2019–20 were $26.6 million, decreased to $25.3 million in 2020–21 and then increased steadily to $29.5 million in 2022–23. When interpreting this trend, it should be noted that insurers may not necessarily be purchasing the same level or type of cover each year. If insurers choose to retain more risk, this may result in lower reinsurance costs if rates are comparable to previous years.

Figure 9.19: Reinsurance costs and recoveries for all SME insurance, northern Australia, 2019–20 to 2022–23, adjusted for inflation

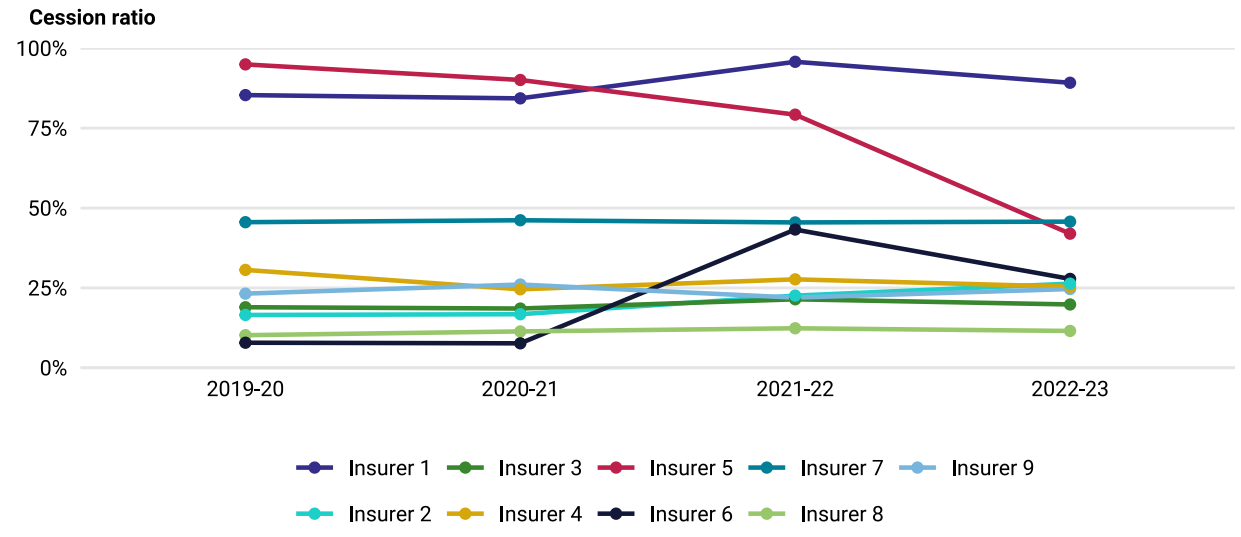


Source: ACCC analysis of data obtained from insurers.

In the 4 years since 2019–20, reinsurance costs have consistently exceeded reinsurance recoveries for SME insurance. The highest reinsurance recovery occurred in 2019–20 ($20.4 million), which is likely associated with claims from the significant and damaging flood event in the Townsville region in early 2019. Reinsurance recoveries have declined in recent years to $1.7 million in 2022–23, likely due to the lack of significant natural disaster events in northern Australia during this period. The relatively short time period means that this data is not necessarily indicative of the long-term trends in reinsurance recoveries for SME insurance in northern Australia.

Figure 9.20 below shows a wide range in the cession ratios across insurers, reflecting the different risk appetites and reinsurance programs of each insurer. Cession ratios are explained in Section 7.2.2. Most insurers maintained a steady cession ratio over the last 4 years, with most insurers having a cession ratio under 50% in the relevant period. This suggests these insurers retained most of their risks rather than choosing to cede the risk to reinsurers.

Figure 9.20: Cession ratio for all SME insurance, northern Australia, 2019–20 to 2022–23



Source: ACCC analysis of data obtained from insurers.

10. Profitability of insurers

Understanding the profitability of supplying insurance in Australia is important for evaluating both the state of the industry and the impact of the pool. If northern Australian regions are consistently unprofitable despite the assistance provided by the pool, insurers will not be encouraged to write policies in regions of medium to high cyclone risk. This in turn will undermine the pool's objectives of lowering the price of insurance and encouraging more insurers to write in these regions. Equally, it is not intended that insurers should benefit from the pool in the form of additional profits. As outlined in Section 1.2, the then government set the expectation that any savings arising from the pool should be passed on to policyholders. For this reason, we will continue to monitor the profitability of home, contents, strata, and SME insurance in northern Australia, using both data from our own information collection and other sources.

The profitability of insurance in northern Australia is one part of the performance of the industry more generally. In reporting to APRA, many insurers have recently reported large profits, with the general insurance industry recording a net profit after tax of $4.6 billion and a return on net assets of 14.2% in 2022–23.[316] The industry also reported a relatively strong underwriting result of $5.7 billion (albeit slightly down on the previous year)[317], due to insurers' increasing premiums in response to higher recent claims costs.[318]

KPMG noted in its General Insurance Industry Review 2023 that there has been a large improvement in the industry's performance, but this has been in a context of low profitability in recent years.[319] The Insurance Council of Australia also recently reported that insurers faced historically low profits from 2020 to 2022, but recently saw improvements in profitability, which it stated were due to a significant turnaround in investment returns and improvements in some commercial lines.[320]

In addition to the home, strata and small business insurance lines that are affected by the pool, these results also include other general insurance product lines, such as motor, commercial, travel and various other classes. While the broader results are useful for context, when the homeowner/householder class of business is considered by itself (noting this is broader than the scope of our data, but includes home and strata insurance), profitability in this segment has been lower. According to APRA data, homeowner/householder insurance for the whole of Australia has recorded underwriting losses for the last 4 years, albeit this measure does not consider investment returns.[321] Underwriting losses have largely been due to the increasing claims costs, including those related to extreme weather events.[322]

In this chapter we examine the profitability of insurers with respect to home and contents, strata and SME insurance, and observe that:

- insurance profits have been poor across Australia in recent years but appear to be recovering sharply
- profits can vary widely between insurers, but the whole industry is affected heavily by natural disasters

316 APRA *Quarterly general insurance statistics*, APRA, June 2023, accessed 24 September 2023.

317 Underwriting result is the premiums an insurer receives minus net incurred claims and underwriting expenses.

318 APRA *Quarterly general insurance performance statistics – highlights*, June 2023, accessed 24 September 2024.

319 KPMG, *Resilience in times of change, General Insurance Industry Review 2023*, accessed 19 September 2023, p 1.

320 Insurance Council of Australia, *ICA Statement – August 2023*, accessed 19 September 2023.

321 KPMG, *GI Insights Dashboard – Product Level*, accessed 26 September 2023.

322 KPMG, *General Insurance Insights Dashboard*, accessed 26 September 2023.

- while historically unprofitable, northern Australia has recently seen higher profit margins than the rest of Australia, which has experienced significant natural disasters.[323]

10.1 Our approach to profitability analysis

We collected financial data for insurance products in scope of the pool from 15 insurers (see Appendix A for more information about the financial data we have collected). We look at trends in insurance profitability over recent financial years, in aggregate, by insurer and by region. High variability in claims costs, and therefore profits, in regions prone to natural disasters means that monitoring performance over longer timeframes is more meaningful.[324] As such, we also use data collected in the Northern Australia Insurance Inquiry to look at profitability trends of home and contents insurance products and strata insurance where possible, for select insurers over a longer period.[325]

We have chosen several metrics (outlined below at Box 10.1) that are commonly used by the insurance industry to measure profitability at different levels. Each measure listed provides a different insight into profitability. For example, the difference between the gross loss ratio and the net loss ratio can indicate the net impact of reinsurance on profits.

Insurer profits are affected by cyclical market conditions, such as inflation, construction cost, labour costs, the performance of the financial sector, and other external factors, such as regulatory requirements and catastrophic events. Some of these factors are outlined in Section 2.3. Additionally, the allocation of financial data to the product types and regions analysed in this chapter relies on various assumptions and methodologies (see Appendix A for more information). Readers should interpret the analysis presented in this chapter in the context of these factors.

Insurers had only begun to enter the pool as at the most recent complete financial year of data available (see Section 3.1 for information about current insurer participation in the pool). This timing means that the results presented in this chapter will not yet reflect outcomes from the pool. The potential impact of the pool on profitability will emerge over the course of our monitoring as more insurers join.

323 ACCC, *NAII final report*, p 108.

324 ACCC, *NAII final report*, p 103.

325 Due to differences in the scope of insurance products between the Northern Australia Insurance Inquiry and our monitoring role, we cannot analyse financial data related to SME insurance products over a longer period. For comparability reasons, the longer-term analyses only include a subset of insurers which provided information as part of the Northern Australia Insurance Inquiry.

Box 10.1: Measures of insurance profitability

- **Gross earned premium**: The sum of insurance premiums earned by an insurance provider, accounting for things such as cancellations and reversals.
- **Net profit (or loss) before tax**: Nominal profit or loss before tax prepared in a format consistent with APRA reporting forms (GRF 310).
- **Profit margin**: Net profit (or loss) before tax divided by gross earned premium.[326]
- **Gross loss ratio**: Ratio of gross incurred claims to gross earned premium. The gross loss ratio provides a view on profitability exclusive of reinsurance and underwriting expenses (such as acquisition costs and commissions). The gross loss ratio provides a view on the profitability of the product itself, unaffected by how profits are split between the primary insurer and reinsurers.
- **Net loss ratio**: Ratio of net incurred claims to net earned premium. The net loss ratio is the gross loss ratio plus the impact of reinsurance premiums and reinsurance recoveries on claims. This ratio is an indicator of the profitability of the product inclusive of reinsurance, but not including underwriting expenses.
- **Combined operating ratio**: Net incurred claims plus underwriting expenses, as a proportion of net earned premium. The combined operating ratio provides one of the most complete performance metrics as it incorporates the above ratios and the expense ratio.[327] The combined operating ratio does not include investment returns or other non-underwriting income and expenses. Insurers with combined operating ratios which marginally exceed 100% can remain profitable overall, depending on the returns on their related investment portfolios. Investment income varies from year to year depending on broader economic conditions and the investment choices of insurers.

10.2 Whole of Australia

This section examines the profitability of home and contents, strata, and SME insurance products in scope of the pool across all of Australia. From the 15 insurers that we collected financial data from, there was over $13 billion of gross earned premium in 2022–23 from these insurance products. Most of this gross earned premium came from residential insurance products (over $10.7 billion), SME insurance products accounted for around $1.6 billion, and strata insurance products just under $1 billion. For context, these insurers reported to APRA over $47 billion of gross earned premium in total over the same period.[328]

10.2.1 Industry profitability

Figure 10.1 below shows that home, contents, strata, and SME insurance profitability at a national level has seen a loss in recent years (adjusted for inflation, around $847 million in 2020–21 and $449 million in 2021–22), but profits have sharply recovered to over $1.3 billion in 2022–23. Stronger investment results and increases in premiums (see Sections 7.1, 8.1 and 9.2) are likely contributing to

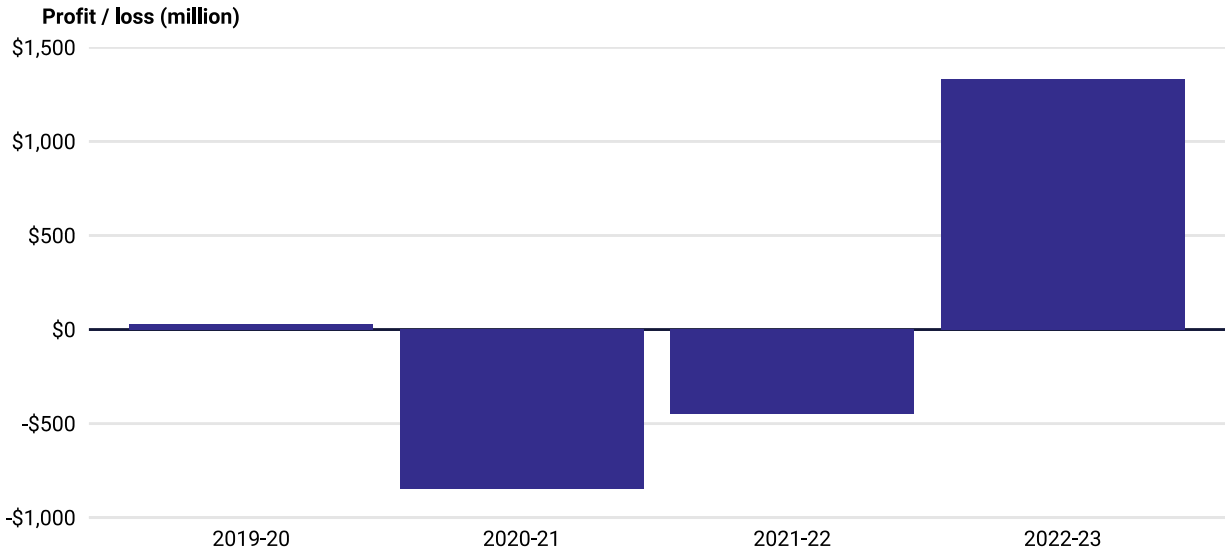
326 Note that this is different from margins discussed in relation to technical premiums in Chapter 4, Section 7.2, Section 8.2, and Section 9.2, which are targets or estimates. Profit margin instead refers to the actual, observed margin.

327 The expense ratio is the ratio of total underwriting expenses to net earned premium.

328 APRA, *Statistics – Quarterly general insurance institution-level statistics database from September 2017 to June 2023*, 24 August 2023, accessed 15 November 2023.

these results.[329] Given the relatively few insurers who were in the pool at the time this information was collected (30 June 2023), we do not expect the pool would be having any impact on these figures.

Figure 10.1: Net profit or loss before tax for all home, contents, strata, and SME insurance, Australia, 2019–20 to 2022–23, adjusted for inflation



Source: ACCC analysis of data provided by insurers.

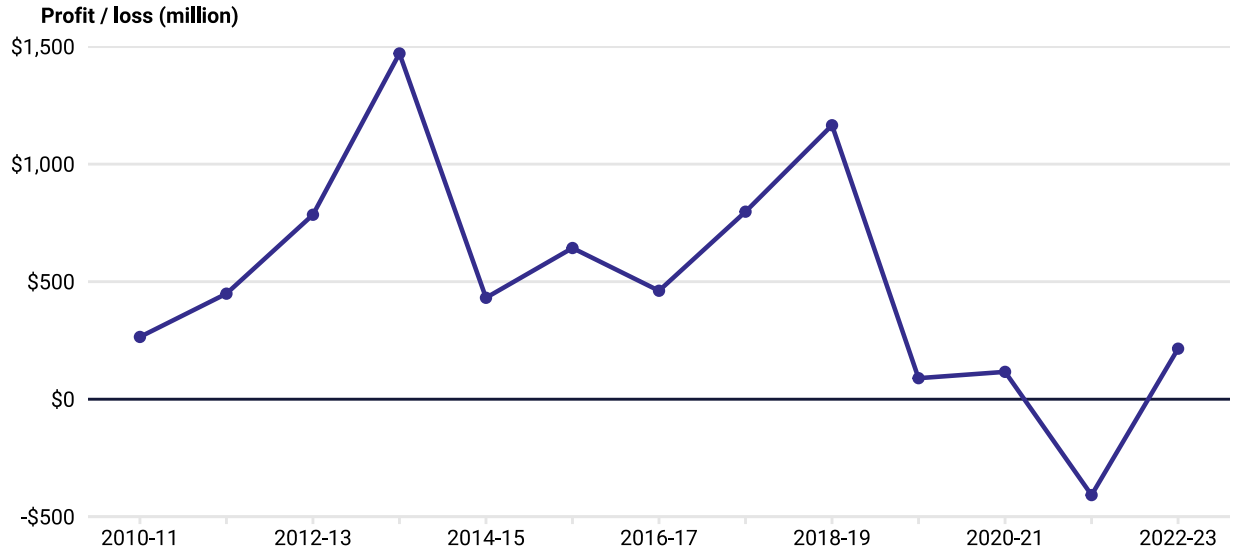
Looking over a longer period, Figure 10.2 below illustrates the longer-term national-level trend in profitability for all home and contents insurance products for a selection of insurers. The figure illustrates that the amount of profit is very volatile (absolute annual changes in inflation adjusted profit ranged from around $27 million to over $1 billion), consistent with the cyclical nature of insurance. While home insurance has experienced underwriting losses in recent years[330], profit results are also impacted by investment returns, which have seen a strong recovery in 2022–23.[331] Documents we obtained from insurers discussed the impacts of significant supply chain disruptions and increased inflation leading in to 2022. This has resulted in higher repair, replacement, and construction costs, and led to claims inflation above headline CPI, contributing to a reduction in home insurance profitability for the entire industry as at June 2022, and in turn higher than average premium increases (see Chapter 7 for more information about the prices and costs of home insurance).

329 APRA, *Quarterly general insurance performance statistics highlights – June 2023*, 24 August 2023, accessed 24 September 2024.

330 KPMG, *General Insurance Insights Dashboard*, KPMG website, 21 September 2023, accessed 26 September 2023.

331 APRA, *Quarterly general insurance performance statistics highlights – June 2023*, 24 August 2023, accessed 24 September 2024.

Figure 10.2: Net profit or loss before tax for all home and contents insurance, Australia, 2010–11 to 2022–23, adjusted for inflation



Source: ACCC analysis of data provided by insurers.

As outlined in Box 10.1 above, the gross loss ratio and net loss ratio are commonly used metrics of insurance profitability. The gross loss ratio provides a view on the profitability of the product itself, unaffected by how profits are split between the primary insurer and reinsurers. The net loss ratio builds on the gross loss ratio by incorporating the effect of reinsurance expenses and recoveries. As an example, if an insurer had a gross loss ratio of 150%, this would suggest the insurer paid out $1.50 in claims for every $1.00 of premium that they collected over the same period. For home insurance a gross loss ratio of around 60% to 65% might be regarded as indicating broadly adequate premium rates.[332] Higher loss ratios than this might be regarded as indicating inadequate premium rates.[333]

Figure 10.3 shows increased gross loss and net loss ratios over the longer term, for a selection of insurers at the national level. The gross loss ratio averaged 67% over the 13-year period, which is only slightly higher than the generally accepted range of 60% to 65% used to assess premium adequacy.[334]

Additionally, the figure below shows the impact of reinsurance on profitability, as the volatility of the net loss ratio between years was reduced as compared to the gross loss ratio. The pool is intended to reduce reinsurance expenses by charging reinsurance premiums without a profit margin.[335] It would also impact reinsurance recoveries on claims in the event of a cyclone. All else equal, this would not change the gross loss ratio, but should reduce the net loss ratio if the insurer writes business in areas of medium to high cyclone risk. The timing of the data shown in Figure 10.3 (as at June 2023) means that any impact of the pool on gross and net loss ratios will not yet be visible, as insurers had only begun to join the pool (as discussed in Section 3.1). Reinsurance costs and recoveries for home, contents, strata, and SME insurance are discussed in Sections 7.2, 8.2, and 9.3, respectively.

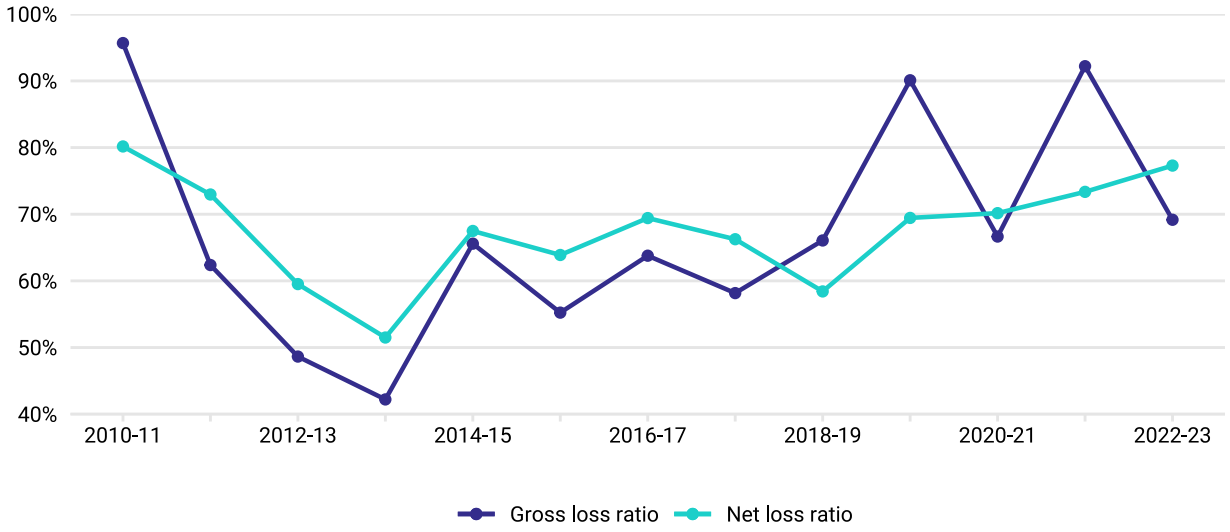
332 Australian Government Actuary (AGA), *Report on home and contents insurance prices in north Queensland*, 3 November 2014, p 12.

333 AGA, *Report on home and contents insurance prices in north Queensland*, 3 November 2014, p 12.

334 AGA, *Report on home and contents insurance prices in north Queensland*, 3 November 2014, p 12.

335 ARPC, *Cyclone pool fact sheet*, accessed 21 September 2023.

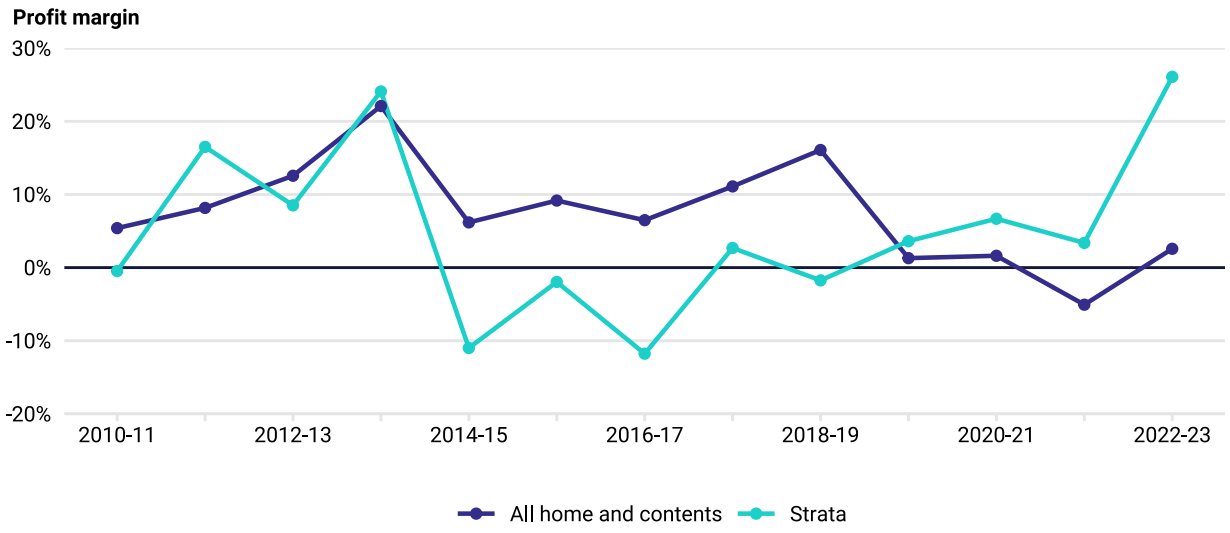
Figure 10.3: Gross loss ratio and net loss ratio for all home and contents insurance, Australia, 2010–11 to 2022–23



Source: ACCC analysis of data provided by insurers.

Figure 10.4 below compares the longer-term national-level trend in profit margins between strata and home insurance products, for a selection of insurers. From 2014–15 to 2018–19, home and contents insurance was generally profitable with an average profit margin of around 10%, while strata insurance saw negative margins, averaging a loss of around 5% over the same period. However, since 2019–20 to 2022–23, strata insurance has outperformed home and contents insurance by an increasing amount each financial year. Margins for strata insurance exceeded those for home and contents insurance by around 2, 5, 8, and 24 percentage points for each of those respective financial years.

Figure 10.4: Profit margin for all home and contents, and strata insurance, Australia, 2010–11 to 2022–23

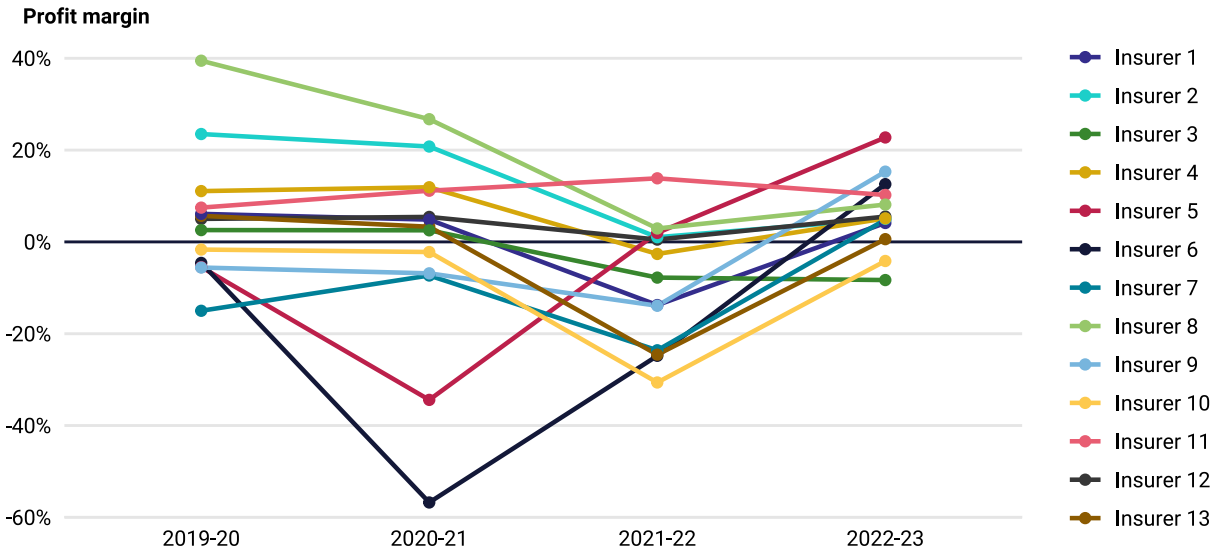


Source: ACCC analysis of data obtained from insurers.

10.2.2 Differences between insurers

In addition to the variability of industry aggregate profits between years, profits can also vary considerably between insurers. Figure 10.5 below shows a range of positive and negative profit margins (from -57% to 39%) in recent years between insurers, for home, contents, strata, and SME insurance products, combined at the national level. Insurers' profit margins can differ depending on how they do business and manage their expenses, for instance which types of products they specialise in and their relative risk exposures. Noting these differences, there has been a general improvement in 2022–23 for most insurers (11 out of 13) as compared to 2021–22.

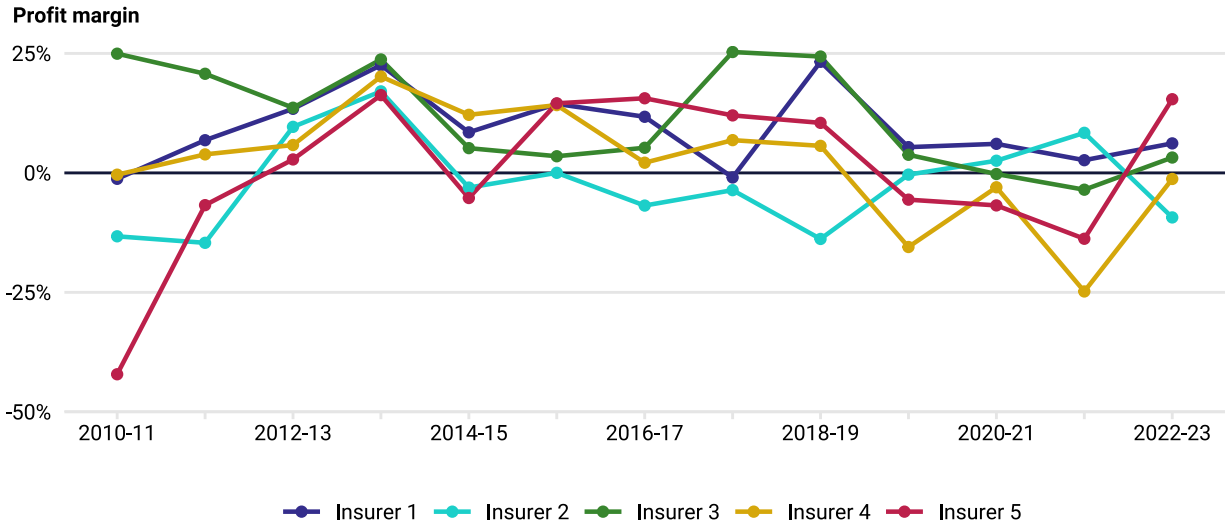
Figure 10.5: Profit margin for all home, contents, strata, and SME insurance, by insurer, Australia, 2019–20 to 2022–23



Source: ACCC analysis of data provided by insurers.

As can be seen in Figure 10.6 below, profit margins can also vary considerably over long periods for all home and contents insurance (ranging from -42% to 25%). However, the national-level profit margins for home insurance products from this selection of insurers appear to be somewhat correlated over the long term. This could be explained by factors beyond individual insurer's direct control that impact profitability, such as significant natural disasters and broader economic conditions. Internal documents we obtained from one large insurer highlight that there was a long period of stability up until the Covid-19 pandemic, but all organisations are now required to navigate the more volatile circumstances of the 'new normal', citing severe weather events and geo-political instability as key disruptions.

Figure 10.6: Profit margin for all home and contents insurance, by insurer, Australia, 2010–11 to 2022–23



Source: ACCC analysis of data provided by insurers.

10.3 Northern Australia

This section examines differences in profitability of home, contents, strata, and SME insurance products in scope of the pool, with respect to regions of northern Australia, using the rest of Australia as a basis for comparison. Comparisons between regions should be interpreted with caution, as insurers have relied on a range of methodologies and assumptions to allocate financial data between these regions (see Appendix A for more information about these caveats).

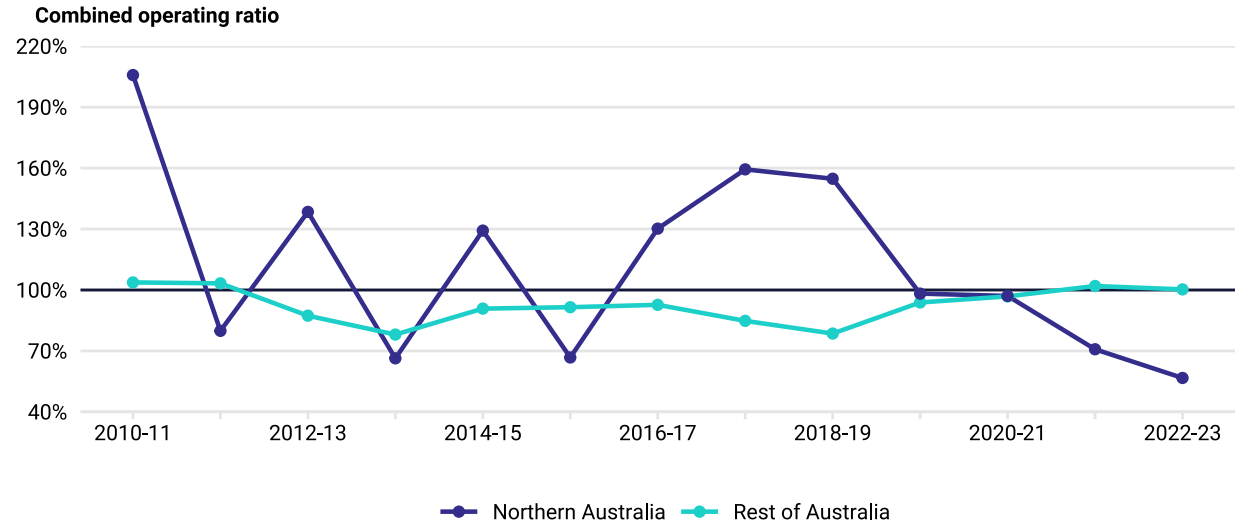
Northern Australia accounts for a relatively small proportion (around 8% in recent years) of the gross earned premium from home, contents, strata, and SME insurance across Australia, based on data obtained from insurers. Within northern Australia, the majority of gross premium is earned in north Queensland, although this has decreased slightly from 81% in 2019–20, to 77% in 2022–23.

Figure 10.7 below shows the combined operating ratio over the longer-term for all home and contents insurance products in northern Australia and the rest of Australia. A combined operating ratio below 100% indicates that underwriting has been profitable, but it does not include investment returns and non-underwriting revenue or expenses. Figure 10.9 indicates that there is more variability in the profitability of northern Australia as compared to the rest of Australia.

Over time, northern Australia has experienced combined operating ratios that were either well above or below those seen in the rest of Australia. For example, 2010–11 saw a combined ratio of 206% in northern Australia, coinciding with Cyclone Yasi which generated $1.4 billion of insured losses at the time.[336] As discussed in Section 4.2.1, insurers often factor historical natural peril claims (such as those due to Cyclone Yasi) into risk modelling, which flows through to premium pricing. Lower combined ratios in northern Australia (as low as 57% in 2022–23) may be due to the generally higher premiums (see Section 7.1), combined with reduced claims costs in those years (for instance, net claims costs for home and contents insurance in northern Australia have reduced considerably between 2017–18 and 2022–23, as shown in Figure 7.16). For comparison, combined ratios for the rest of Australia ranged between 78% and 104% over the period from 2010–11 to 2022–23.

336 Swiss Re, *Resilience through the lens: Ten years on, Tropical Cyclone Yasi*, accessed 26 September 2023.

Figure 10.7: Combined operating ratio for all home and contents insurance, by region, 2010–11 to 2022–23



Source: ACCC analysis of data obtained from insurers.

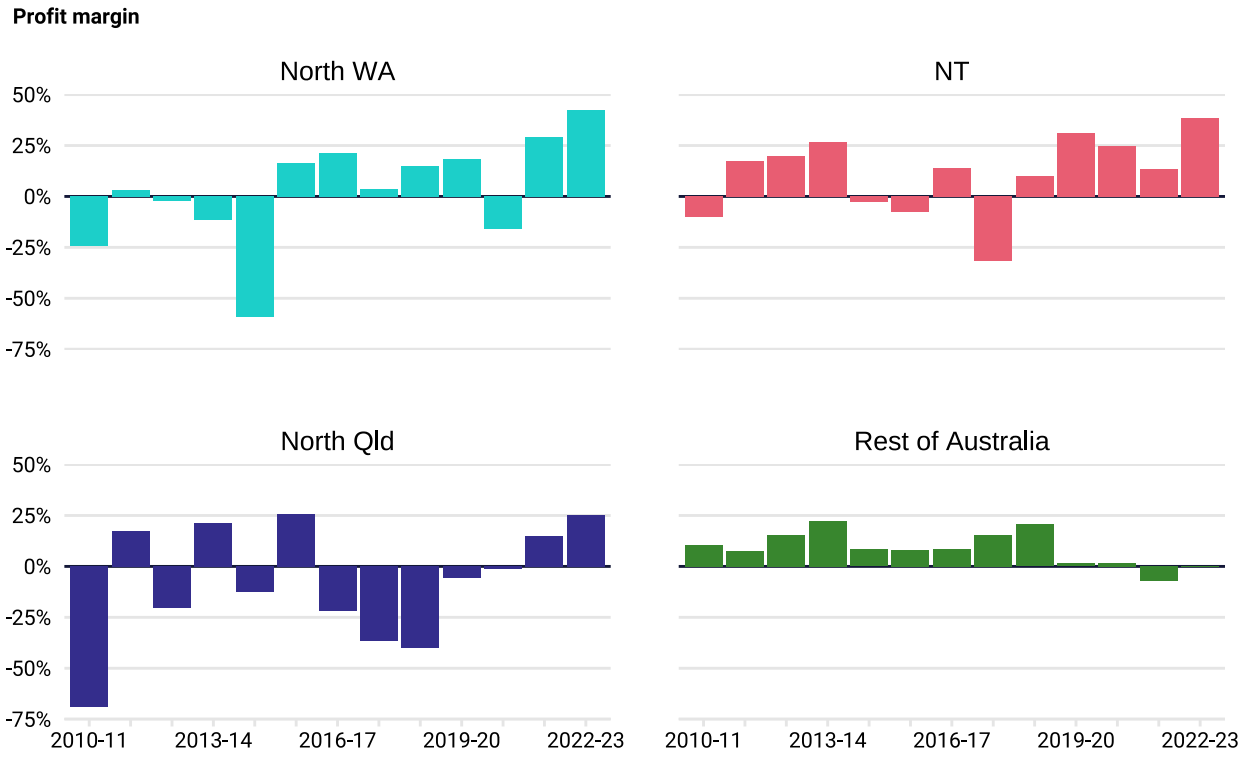
In recent years, underwriting profitability has improved in northern Australia and worsened elsewhere. This is perhaps indicative of the region-specific impacts of natural catastrophes on insurance profitability. Many recent natural catastrophes have occurred outside of northern Australia. For example, according to the NSW Rural Fire Service, the 2019–20 bushfire season destroyed nearly 2,500 homes in New South Wales.[337] The Insurance Council of Australia has also highlighted that the 2022 south-east Queensland and northern New South Wales flood cost the insurance industry over $5 billion, making it the second most costly extreme weather event in Australia's history.[338]

Figure 10.8 below shows the profit margins of regions in northern Australia and the rest of Australia, for all home and contents insurance products. Consistent with the outcomes in Figure 10.7, the profit margins in northern Australia appeared more volatile, with large variations in profit margins year on year (varying by up to 86 percentage points between consecutive years). The rest of Australia had a steadier trend of mostly positive profit margins (ranging by 29 percentage points over the period from 2010–11 to 2022–23). Notably, regions of northern Australia have recently had greater profit margins than the rest of Australia (in 2022–23; 43% in north Western Australia, 38% in the Northern Territory, 25% in north Queensland, and breakeven in the rest of Australia). The recently improved profitability of northern Australia contrasts with sizable negative margins (as great as -69%) in those regions in earlier periods.

337 NSW Rural Fire Service, *BUSH FIRE bulletin [PDF 8.9MB]*, accessed 21 September 2023.

338 Insurance Council of Australia, *Insurance Catastrophe Resilience Report 2021–22 [PDF 3.5MB]*, accessed 21 September 2023.

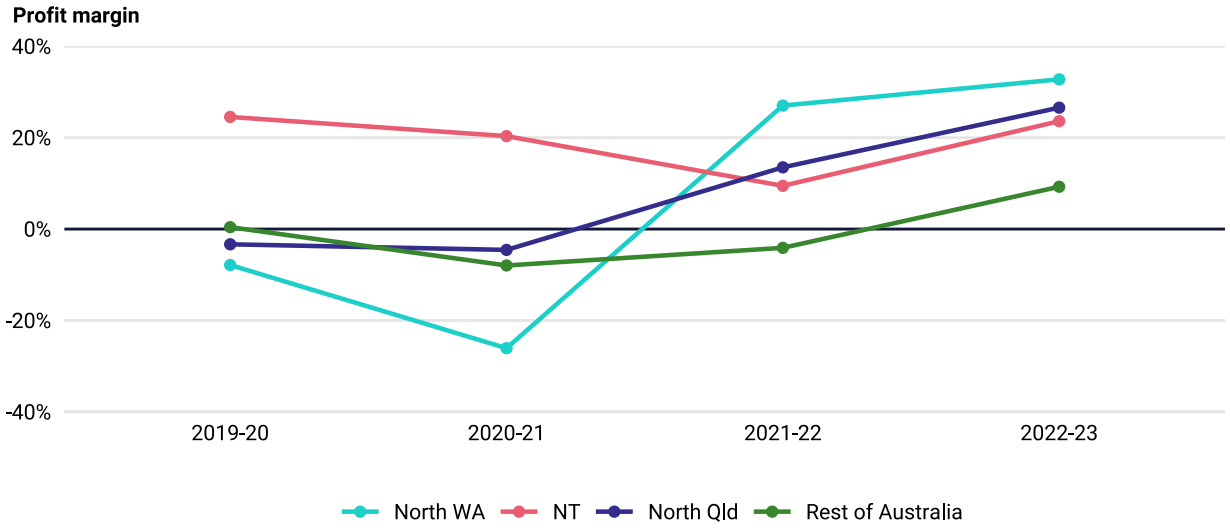
Figure 10.8: Profit margin for all home and contents insurance, by region, 2010–11 to 2022–23



Source: ACCC analysis of data obtained from insurers.

Figure 10.9 below shows the profit margins for all home, contents, strata, and SME insurance products (for SME policies with a sum insured that does not exceed $5 million) for the financial years 2019–20 to 2022–23. Margins in 2019–20 were -8% in north Western Australia, 25% in the Northern Territory, -3% in north Queensland, and breakeven in the rest of Australia. In 2022–23 these had mostly increased, with north Western Australia at 33%, the Northern Territory at 24%, north Queensland at 27%, and the rest of Australia at 9%. One insurer has noted that the pool may reduce the volatility of margins in the future. This is because all eligible cyclone risk is transferred to the pool, whereas previously the losses from a large cyclone event in northern Australia would have been borne by the insurer, undermining its profits. While there has not yet been an impact from the pool on profit margins as at June 2023, we will continue to monitor trends in profit margins and other metrics of profitability over the course of our monitoring role.

Figure 10.9: Profit margin for all home, contents, strata, and SME insurance, by region, 2019–20 to 2022–23



Source: ACCC analysis of data obtained from insurers.

Appendix A: Data collection and methodology

We used our compulsory information gathering powers under section 95ZK of the *Competition and Consumer Act 2010* to obtain information, data and documents from insurers. These insurers supply home and contents, strata and small business insurance in regions considered to be at risk of cyclone and cyclone-related flood damage in Australia.

This appendix describes our approach to data collection, quality assurance and methodology, outlining any data limitations where relevant. We also describe differences or changes between the data approach taken for this report and the approach used in our first report and the Northern Australia Insurance Inquiry.

Data collection

To inform the analysis and observations in this report, we collected information from 21 insurers about the types of insurance policies that are covered by the pool. These policies include:

- residential home and/or contents policies
- commercial strata and small to medium enterprise business insurance up to a total sum insured of $5 million across property, contents and business interruption
- residential strata (where 50% or more of the floor space is used mainly for residential purposes).

Where possible, we have compared information we have collected against that previously collected during the Northern Australia Insurance Inquiry. Because the Northern Australia Insurance Inquiry had a different focus, it sought information from a subset of the insurers that we have requested information on for this report, as shown in the table below.

Table A: Insurers we collected information from

	This report	NAII final report
AAI Limited (Suncorp)	✓	✓
Achmea Schadeverzekeringen N.V.	✓	
AIG Australia Limited	✓	
Allianz Australia Insurance Limited	✓	✓
Ansvar Insurance Limited	✓	
Auto & General Insurance Company Limited	✓	
Chubb Insurance Australia Ltd	✓	
Defence Service Homes Insurance Scheme	✓	
Guild Insurance Limited	✓	
The Hollard Insurance Company Pty Ltd	✓	
Hollard Insurance Partners Limited (formerly Commonwealth Insurance Limited)[339]	✓	✓
Insurance Australia Limited and Insurance Manufacturers of Australia Pty Ltd (together, Insurance Australia Group)	✓	✓
Liberty Mutual Insurance Company	✓	
Pacific International Insurance	✓	
QBE Insurance (Australia) Limited	✓	✓
RAC Insurance Pty Ltd	✓	
RACQ Insurance Limited	✓	✓
Sure Insurance Pty Ltd[340]	✓	
Westpac[341]		✓
Youi Pty Ltd	✓	✓
Zurich Australian Insurance Limited	✓	

With respect to time series data we present in this report, some figures may only include insurers that we collected data from as part of the Northern Australia Insurance Inquiry to ensure comparability over time.

Where time series information is presented, there may be small changes to data, definitions or calculations between the information we have collected and that collected during the Northern Australia Insurance Inquiry, particularly across different insurers. For these reasons, comparisons over time should be interpreted with caution.

339 Our first insurance monitoring report contains data from Commonwealth Insurance Limited for a period prior to its acquisition by Hollard Group on 30 September 2022. From 1 October 2022, Commonwealth Insurance Limited has been renamed Hollard Insurance Partners Limited. Hollard Insurance, *New Insurance Partnership: About Hollard and the Commonwealth Bank*, Hollard website, n.d. accessed 28 June 2023.

340 Sure Insurance Pty Ltd is not an insurer, but a managing general agency (MGA) underwriting policies for its product issuers Liberty Mutual Insurance Company and Pacific International Insurance. Data on insurance policies and claims used in this report considers the 3 entities together as one insurer.

341 Westpac General Insurance Limited and Westpac General Insurance Services Limited were acquired by Allianz on 1 July 2021.

Information about small business insurance, with the exception of a specific case study, was not collected in the Northern Australia Insurance Inquiry. This means that our analysis of small business insurance is limited to more recent time periods as we do not have historical Northern Australia Insurance Inquiry data to compare against.

Where we refer to home insurance products, this includes residential building insurance, residential contents insurance and residential combined home and contents insurance. Similarly, where we refer to small business or small to medium enterprise (SME) insurance products, this includes SME building insurance, SME contents insurance, SME combined building and contents insurance, and SME business interruption insurance.

Types of information collected

We collected information from insurers on 3 primary data sets, along with supporting information about those data sets. We intend to continue these data collections over the course of our monitoring role.

Policy level data

We collected granular policy level data from insurers for the first time as part of our insurance monitoring role. Broadly, we sought information about each policy on the location of the property, policy excess, technical premium components, premium adjustments and the retail premium. We collected this data for policies in effect as at 30 September 2022 (a time before any insurers had joined the pool) for most insurers in our sample. Two insurers provided data for policies in effect as at a different reference date due to system constraints.

Insurers also provided accompanying documents explaining the calculations and methodology used, and assumptions made to respond to the items.

Some insurers could not provide certain information requested due to factors including system constraints or lack of availability. Where information could not be provided, insurers indicated the reasons why it was not provided.

Aggregated policy and claims data

We sought postcode level policy and claims data for the 2022–23 financial year, to supplement the 2021–22 data collected as part of first report, and previous data collected as part of the Northern Australia Insurance Inquiry (which covered 2007–08 to 2018–19 financial years).[342] Broadly, the information requested relates to descriptive statistics for excess, number of risks written, sum insured, gross written and earned premiums, claims, taxes and levies and retail premium metrics.

We note that the 2019–20 and 2020–21 financial years were not collected, and therefore data is not available for those years. While the number of insurers we sought information from differs across the collections for our current monitoring role and the Northern Australia Insurance Inquiry, we have undertaken further analysis to ensure the accuracy and reliability of our findings.

Insurers provided accompanying documents explaining the calculations and methodology used, and assumptions made to respond to the items.

Financial data

We sought region level financial data for the 2022–23 financial year, to supplement the 2019–20, 2020–21 and 2021–22 data collected for our first report. Older versions of this dataset were first

342 As noted earlier, SME data was not collected as part of the Northern Australia Insurance Inquiry.

collected as part of the Northern Australia Insurance Inquiry, which covered the 2007–08 to 2018–19 financial years.[343]

We requested information aggregated to regions within northern Australia (split by state or territory) and the whole of Australia. Broadly, we sought information relating to revenues and costs to assist in our assessment of insurer costs and profitability. Insurers also provided accompanying documents explaining the calculations and methodology used, and assumptions made to respond to the items. The various methodologies and assumptions used by insurers to allocate financial data mean that these analyses should be interpreted with some caution. Some insurers could not provide certain information due to factors including system constraints, lack of availability of particular data items, or lack of an appropriate disaggregation methodology to provide the information at the required region level and product type. Where information could not be provided, insurers indicated the reasons why it was unable to be provided.

Where insurers could not provide the information at the required region level or product type, they provided the items requested at a more aggregated level. These limitations have meant that we have excluded certain insurers from particular analysis involving region or product type splits.

Quality assurance

We examined responses across all 3 data collections for inconsistencies and errors to ensure that the data meets the quality standards required to be included as part of this report. For example, we checked that:

- the methodology and assumptions used by insurers appear logical and reasonable
- data was provided in the right format and contained valid and complete information
- the totals provided are the sum of the various individual components
- numerical signs made sense, such as positive revenue values
- values seem logical and within expected ranges
- values for items that are interrelated appear logical.

Our checks identified data quality issues and data abnormalities for several insurers. In each case we contacted insurers for clarification and, where appropriate, updated data was provided. We repeated checks on any new data provided.

Methodology and classifications

Geographic classifications

Across our report, we present our data in various geographic classifications. These include:

- Northern Australian regions (split by state or territory)
- Australian Bureau of Statistics (ABS) Statistical Area 3 (SA3) region basis for all geospatial maps
- Catastrophe Risk Evaluation and Standardising Target Accumulations (CRESTA) zones for analysis involving selected cities and towns.

343 As noted earlier, SME data was not collected as part of the Northern Australia Insurance Inquiry.

In this report, we have defined northern Australia as all of the Northern Territory and those parts of Queensland and Western Australia that intersect with or are north of the Tropic of Capricorn.[344]

We selected SA3 as the geographic level for the geospatial maps as they cluster areas that have similar geographic and socio-economic characteristics. More information on statistical areas can be found on the ABS website.

We utilised a combination of low resolution and high resolution CRESTA zones to produce the values seen in 'select cities' figures. CRESTA zones are part of an international geographic zoning system used by the insurance industry. High resolution CRESTA zones are generally smaller geographic regions. Smaller cities or towns such as Port Hedland or Karratha would typically align with one high resolution CRESTA zone. Low resolution CRESTA zones, on the other hand, are generally defined as larger geographic regions. Larger cities like Melbourne or Townsville would typically be one low resolution CRESTA zone. The cities presented in the report are not exhaustive but we have sought to provide a spread across states and territories of particular interest.

Insurance availability

Chapter 6 discusses insurance availability and presents analysis on the number of insurers with more than 10 policies in effect by region. We considered a minimum of 11 policies from an insurer in an area to be a reasonable presence, noting that the regions, cities and towns vary greatly across the country in the number of homes, strata title properties and small businesses in scope of the pool.

It is important to note that there may be insurers offering policies in the regions, cities or towns presented that did not have any policies in effect as at the reference date. There may also be other insurers offering these types of policies that we have not collected data from. Because we have focused our collection of data from insurers required to join the pool, there may be insurers providing relevant insurance products outside northern Australia which are not captured in this analysis. However, it is likely to be a small number of policies not captured. The insurers included in our data collection collectively accounted for over 86% of gross written premium for general insurance institutions for the financial year ending June 2023.[345]

Price and breakdown of retail premiums

Average prices

We present insurance prices in multiple ways in this report. Where time series information have been presented, we have used our aggregated policy and claims collection, which continues the collection established during the Northern Australian Insurance Inquiry. All other analysis relies on our policy level data collection. Because these 2 datasets were collected at different points in time, the average premiums and average premiums per sum insured values presented in the maps may not align with the values presented in time series data (for example see Figure 7.1 in Section 7.1.1).

Distribution of premiums

We produced a number of distribution, or 'box and whisker' figures, or box plots, within Chapters 7, 8 and 9 using our policy level data. Each box plot shows the range of values for a set of premiums using the following statistics:

- 5th percentile whisker
- 25th percentile values (lower line)

344 Department of Infrastructure, Transport, Regional Development, Communications and the Arts, *Office of Northern Australia,* Department of Infrastructure, Transport, Regional Development, Communications and the Arts website, accessed 6 October 2023.

345 Australian Prudential Regulation Authority, *Quarterly general insurance institution – level statistics as at 30 June 2023,* APRA website, accessed 6 September 2023.

- median values (middle line)
- 75th percentile values (upper line)
- 95th percentile whisker.

The whiskers show 5th and 95th percentile rather than minimum and maximum values to strike a balance between showing a wide range of consumer outcomes whilst ensuring that the scale within each figure is not severely impacted by extreme values. Where relevant, we have identified some of the outlier ranges within the text of the report.

Where necessary, we have removed obviously erroneous values from the dataset before producing these figures, such as negative, $0 and $1 average premium observations.

Selection of 'typical' excess and sum insured

We explore average premium outcomes for policyholders with 'typical' excess and/or sum insured values within Chapters 7, 8 and 9. These ranges of excess and sum insured values were selected by taking approximately the middle 50% of records across the data set and identifying the excess and sum insured values that these policies tended to have, for each product type. We note that while these ranges represent 'typical' ranges found across most policies for each product type, they may not represent the typical ranges for each region or area. For instance, we selected $500 to $1,000 as the 'typical' excess selected by residential combined home and contents insurance policyholders. However, for north Queensland, the median excess paid was between $1,000 and $2,000.

Average retail premium breakdowns

We used a combination of policy level and aggregate policy and claims data to create average retail premium breakdowns (see Figures 7.15, 8.16 and 9.15). Specifically, we apportioned the movements between the retail premium and the technical premium using the policy level data, and applied it to the average premium obtained from the aggregated policy and claims data. These averages were generally comparable. However, we note that only records with complete information (in other words, no missing retail premium breakdown information) were included for analysis. Noting slight differences in the collection method and timing, findings should be interpreted with caution.

We have undertaken this approach to ensure consistency between the average retail premium values reported in other figures and the values presented in Figures 7.15, 8.16 and 9.15.

Improvements from our first report

A number of refinements have been made to our approach in this report compared to our first report. We have included a greater number of insurers for the 2021–22 financial year compared to what was presented in our first report, which was limited to the insurers included in the Northern Australia Insurance Inquiry. This has provided a more complete assessment of average premiums across regions for 2021–22. We have also made some refinements to our calculation of average premiums and average premiums per sum insured, including addressing some inconsistencies in the handling of tax and levies in the retail premium. Finally, we have further refined our approach to adjusting for the effects of inflation, as explained further below.

Adjusting for inflation

We present financial figures, including premiums, for previous years in real terms (in 2022–23 dollars). This removes the effect of general price inflation on price trends, and allows for analysis of real movements. Values have been indexed to 2022–23 using the average All Groups Australia Consumer Price Index for the 4 quarters of each financial year.[346] This is a refinement from the previous approach in our first report, where we used the change in the All Groups Australia Consumer Price Index between June quarters of each financial year.

346 Australia Bureau of Statistics, *Consumer Price Index, Australia, June Quarter 2023*, ABS website, accessed 6 October 2023.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