



Australian
Competition &
Consumer
Commission

Determination

Application for authorisation

lodged by

Insurance Council of Australia

in respect of

an agreement between its members to adopt, on a voluntary basis, a common definition of “inland flood”

Date: 3 September 2008

Authorisation no.: A91086

Public Register no.: C2008/484

Commissioners: Samuel
Kell
Court
King
Martin
Walker

Summary

The ACCC has decided to deny authorisation to the Insurance Council of Australia's proposed common definition of inland flood.

The ACCC recognises the efforts by Government and industry aimed at improving both the availability of flood insurance and consumer understanding of flood issues.

The ACCC encourages the Insurance Council, its members and interested stakeholders to consider refinements to the proposed common definition which may alleviate the concerns identified by this determination. The ACCC notes that its decision in this matter does not prevent the insurance industry from seeking authorisation of a revised proposal in the future.

The authorisation process

The Australian Competition and Consumer Commission (ACCC) can grant immunity from the application of the competition provisions of the *Trade Practices Act 1974* (the Act) if it is satisfied that the benefit to the public from the conduct outweighs any public detriment. The ACCC conducts a public consultation process to assist it to determine whether a proposed arrangement results in a net public benefit.

The application for authorisation

On 20 March 2008, the Insurance Council of Australia (Insurance Council) lodged application A91086 with the ACCC, seeking authorisation of an agreement between its members to adopt, on a voluntary basis, a common definition of "inland flood".

The definition of "inland flood" proposed by the Insurance Council is:

Inland Flood is the covering of land that is not normally under water by:

- *water that overflows or escapes from a naturally occurring or man made inland watercourse (such as a river, creek, canal or storm water channel) or a water pool (such as a lake, pond or dam), whether it is in its original state or it has been modified; or*
- *water released from a dam whether it be accidentally released or intentionally released to control, mitigate, regulate, or otherwise respond to excess water, or*
- *water that cannot drain or run off as a result of water that is overflowing or escaping from an inland watercourse or water pool preventing the escape of water.*

Background

In recent years major flooding events in Australia have raised strong community concerns about the extent and availability of cover for flood damage. The effects of flood can be devastating for the individual consumer and come at a high cost to all Australians - actuarial estimates place the average total annual cost of residential flood damage in Australia at \$350 million. Individual flooding events can however have a far more significant economic and social impact.

A number of reports have highlighted a lack of consumer awareness in respect of flood cover – in particular (i) whether policies offer cover for flood damage; and (ii) the importance of the distinction between flood and other storm damage.

Key issues raised during the course of the ACCC’s consultation process

Key issues for consideration raised during the course of the ACCC’s consultation process were:

- the potential for a standard definition to promote greater recognition and understanding of flood insurance amongst consumers
- the potential for a standard definition to result in the simplification and harmonisation of complex contractual terms dealing with flood insurance
- concerns that the Insurance Council’s proposal may restrict competition between insurers in the provision of flood cover
- concerns that the Insurance Council’s proposal may reduce the current level of product differentiation between insurers in relation to flood cover
- concerns as to the effectiveness of the Insurance Council’s proposed communications campaign
- concerns about the terminology put forward by the Insurance Council, in particular that the proposed common definition introduces new terminology, expands established concepts and seeks to diminish the doctrine of proximate cause
- concerns that the Insurance Council’s proposed common definition, by potentially increasing consumer confusion, may inhibit the ability of consumers to make informed choices leading to an increased risk that consumers may obtain cover which is inappropriate for their needs
- concerns that, in the absence of strong industry support for a move to greater harmonisation of contractual terms dealing with flood insurance, the Insurance Council’s proposal would deliver limited benefits to consumers.

ACCC assessment

A standard definition of flood has the potential to promote greater understanding of the nature of flood insurance amongst consumers. This greater understanding is likely to result in a range of public benefits, including promoting improvements in the appropriateness of cover obtained by consumers by providing them with the resources necessary to allow them to make better informed decisions.

In this respect consumer representatives have noted that a standard definition for flood is likely to result in a reduction in consumer confusion, more informed decision making and fairer coverage for consumers, including better informed pricing decisions.

In its draft determination the ACCC considered that the Insurance Council’s proposed common definition was *not* likely to deliver benefits to the public which would outweigh its likely anti-competitive detriment. The ACCC however considered that, with the imposition of conditions, it was more likely that the net public benefit test could be met and accordingly proposed to grant conditional authorisation to the Insurance Council and its members.

Having had regard to the additional materials provided to it by consumer groups, the Australian Securities and Investments Commission and the National Insurance Brokers Association following the draft decision, the ACCC can no longer be satisfied that the imposition of conditions would alleviate its concerns. In particular the ACCC notes that the potential for the proposed common definition to introduce new concepts and to increase consumer confusion is not a concern which can be addressed by the imposition of conditions.

The ACCC has therefore decided to **deny** authorisation to application A91086.

The ACCC recognises the efforts by Government and industry aimed at improving both the availability of flood insurance and consumer understanding of flood issues. The ACCC also recognises that this is a complex issue and encourages the Insurance Council and its members to continue working with consumer groups and other interested stakeholders.

The ACCC encourages the Insurance Council, its members and interested stakeholders to consider refinements to the proposed common definition which may alleviate the concerns identified by this determination.

The ACCC notes that its decision in this matter does not prevent the insurance industry from seeking authorisation of a revised proposal in the future.

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List of abbreviations

ACCC	Australian Competition and Consumer Commission
ASIC	Australian Securities and Investments Commission
COAG	Council of Australian Governments
Insurance Council	Insurance Council of Australia
NIBA	National Insurance Brokers Association
The Act	<i>Trade Practices Act 1974 (Cth)</i>

1. Introduction

Authorisation

- 1.1 The Australian Competition and Consumer Commission (the ACCC) is the independent Australian Government agency responsible for administering the *Trade Practices Act 1974* (the Act). A key objective of the Act is to prevent anti-competitive conduct, thereby encouraging competition and efficiency in business, resulting in a greater choice for consumers in price, quality and service.
- 1.2 The Act, however, allows the ACCC to grant immunity from legal action in certain circumstances for conduct that might otherwise raise concerns under the competition provisions of the Act. One way in which parties may obtain immunity is to apply to the ACCC for what is known as an ‘authorisation’.
- 1.3 The ACCC may ‘authorise’ businesses to engage in anti-competitive conduct where it is satisfied that the public benefit from the conduct outweighs any public detriment.
- 1.4 The ACCC conducts a public consultation process when it receives an application for authorisation. The ACCC invites interested parties to lodge submissions outlining whether they support the application or not, and their reasons for this.
- 1.5 After considering submissions, the ACCC issues a draft determination proposing to either grant the application or deny the application.
- 1.6 Once a draft determination is released, the applicant or any interested party may request that the ACCC hold a conference. A conference provides all parties with the opportunity to put oral submissions to the ACCC in response to the draft determination. The ACCC will also invite the applicant and interested parties to lodge written submissions commenting on the draft.
- 1.7 The ACCC then reconsiders the application taking into account the comments made at the conference (if one is requested) and any further submissions received and issues a final determination. Should the public benefit outweigh the public detriment, the ACCC may grant authorisation. If not, authorisation may be denied. However, in some cases it may still be possible to grant authorisation where conditions can be imposed which sufficiently increase the benefit to the public or reduce the public detriment.

The application for authorisation

- 1.8 On 20 March 2008, the Insurance Council of Australia (Insurance Council) lodged application for authorisation A91086 with the ACCC.
- 1.9 The Insurance Council applied for authorisation of an agreement between its members to adopt, on a voluntary basis, a common definition of “inland flood”.
- 1.10 The Insurance Council has sought authorisation for a period of five years.

Draft determination

- 1.11 On 3 July 2008 the ACCC issued a draft determination proposing to grant conditional authorisation to the Insurance Council's proposal for a period of two years.
- 1.12 The ACCC invited submissions from interested parties commenting upon the draft determination, submissions received by the ACCC are available from its public register and are reflected in chapter 6 of this determination. The ACCC also convened a pre decision conference on 4 August 2008. The submissions made at the conference are reflected in chapter 6 of this determination and a record of the conference is also available from the ACCC's public register.

Chronology

- 1.13 Table 1.1 provides a chronology of significant dates in the consideration of this application.

Table 1.1: Chronology of application for authorisation A91086

DATE	ACTION
20 March 2008	Application for authorisation lodged with the ACCC.
18 April 2008	Closing date for submissions from interested parties in relation to the substantive application for authorisation.
15 May 2008	Submission received from the Insurance Council in response to interested party submissions.
27 June 2008	Submission received from the Insurance Council providing further information.
3 July 2008	Draft determination issued.
21 July 2008	Date by which pre decision conference must be requested.
24 July 2008	First closing date for submissions responding to the draft determination.
4 August 2008	Pre decision conference held.
8 August 2008	Second closing date for submissions responding to the draft determination.
19 August 2008	Submission received from the Insurance Council in response to interested party submissions.
3 September 2008	ACCC determination issued.

2. Background to the application

2.1 This chapter provides relevant background information regarding the ACCC's consideration of the application for authorisation lodged by the Insurance Council.

The applicant¹

2.2 The Insurance Council is the representative body of the general insurance industry in Australia. The Insurance Council has 58 member groups including insurance companies, reinsurance companies, underwriters, intermediaries, and agencies from the private and public sectors.

2.3 The Insurance Council was established to act as the peak body for general insurance companies in Australia licensed under the *Insurance Act 1973*.² The Insurance Council's main objectives are set out on its website as:

- represent members' interests in both domestic and international issues;
- represent the general insurance sector to Government and the community;
- anticipate, and assist the industry to meet, the needs of consumers and the community generally;
- improve the industry's image;
- promote community awareness of the role and benefits of insurance;
- encourage improved service standards across the insurance sector and promote appropriate self-regulation;
- to promote private sector provision of insurance services; and
- to effectively and efficiently manage Insurance Council of Australia resources.³

2.4 The Insurance Council's members represent more than 90% of total premium income written by private sector general insurers.

2.5 Insurance Council members provide non-life insurance products including those purchased by individuals (e.g. home and contents insurance, travel insurance and motor vehicle insurance) and those purchased by business and large organisations (e.g. public liability insurance, workers compensation insurance, commercial property insurance and directors and officers insurance).

¹ Unless otherwise indicated, the information in this section is taken from Insurance Council of Australia, Submission in support of application for authorisation A91086, 20 March 2008.

² www.insurancecouncil.com.au, accessed 10 May 2008.

³ Ibid.

The insurance industry

2.6 Insurance is the commercial relationship by which an insurance company agrees to pay the insured a sum of money as compensation on the occurrence of a specified event causing loss to the interests of the insured. The insured party pays an amount, known as a 'premium', in consideration.⁴

2.7 In Australia, the Australian Prudential Regulation Authority (APRA) has responsibility for the licensing and prudential regulation of general insurance companies.⁵ The products provided by general insurance companies can be divided into nine main classes:

- domestic motor
- home
- commercial third party (CTP)
- accident and travel
- fire and industrial special risk
- commercial motor
- public and product liability
- marine and
- other.

2.8 Statistics published by APRA⁶ note that over the 2006/2007 financial year general insurance products were offered by 111 direct insurers, earning gross premium revenue of \$28.0 billion. Domestic motor vehicle was the largest component of total direct gross premium revenue at \$5.209 billion or 21.8%, while homeowners/householders insurance comprised approximately \$3.773 billion or 13.4%. New South Wales and the Australian Capital Territory account for the largest share of general insurance total gross premium revenue at 42.3%.

2.9 In terms of market concentration the top 5 groups of insurance companies hold 91% of personal business (comprising domestic motor vehicle and homeowners/householders policies). APRA notes that in the period 2006/2007, NSW/ACT had the highest level of market concentration in personal business with the top five groups accounting for 94% of total gross premium revenue.

⁴ Business Law, 11th Edition, Peter Gillies, 2003 at page 716.

⁵ APRA is also responsible for the prudential regulation of banks, superannuation funds, credit unions, building societies and friendly societies.

⁶ *Statistics - Half Yearly General Insurance Bulletin*, APRA, June 2007 (Revised 25 February 2008).

- 2.10 The major sales avenue for insurance is through companies' own outlets, or through intermediaries – namely, agents or brokers. Brokers carry on the business of arranging contracts of insurance on behalf of policyholders and also sell insurance on behalf of one or more insurers.
- 2.11 Entry into the general insurance industry requires entities to:
- gain knowledge of their targeted market segments
 - enter at a level sufficient to claim the necessary economies of scale
 - attract necessary capital
 - establish distribution channels and
 - obtain staff with the skills to write for the business.
- 2.12 In its 2005 report *Getting home insurance right - A report on home building underinsurance* the Australian Securities and Investments Commission (ASIC) noted that the level of underinsurance in Australia is high, with surveys suggesting that between 27% and 81% of consumers were underinsured by 10% or more against current rebuilding costs.

Flood insurance

- 2.13 In its June 2000 report *Consumer understanding of flood insurance* ASIC provided the following general definition of 'flood damage'
- flood damage refers to the inundation of a property by water which overflows from a natural watercourse, while storm and tempest damage refers to the inundation of a property by water as the result of a storm*
- 2.14 ASIC further noted that the majority of disputes concerning flood insurance claims stemmed from a lack of understanding amongst consumers as to the effect of their policy. Key areas of confusion were that
- most policies do not cover damage to a property caused by the inundation of water flowing from a natural watercourse;
 - most policies do not cover damage where the property is inundated by mingled waters from the storm and from the overflow of a natural watercourse (unless most of the damage is caused by stormwater); and
 - most policies do not cover damage where the proximate cause of the damage is another phenomenon, such as earth movement, even though this may itself have been caused by water from a storm.
- 2.15 It was also noted by ASIC that flood insurance is not available in many areas in Australia. In responding to this issue the insurance industry has argued that the provision of flood insurance relies largely on the availability of adequate flood mapping and other information to enable the underwriting of risks.

2.16 In the August 2002 report to the Council of Australian Governments (COAG) on *Natural Disasters in Australia - reforming mitigation, relief and recovery arrangements* (the COAG Report) a number of recommendations were made aimed, in part, at reducing the exposure of the insurance industry to natural disaster losses and to make insurance more attractive and affordable. In respect of flood damage, key recommendations included

- a five-year national system of rigorous disaster risk assessments
- improved data collection, research and analysis
- Commonwealth, State and Territory natural disaster mitigation strategies
- action to ensure more effective statutory land use planning, development and building control regimes taking account of natural hazards
- a five-year Disaster Mitigation Australia Package, consisting of a new Disaster Mitigation Programme and continuation of the Regional Flood Mitigation Programme, and
- a national strategy of community awareness, education and warnings.

Recommendation 35 sets out two preconditions for eligibility for funds for flood mitigation, proposing that:

- based on the principle of ‘community right to know’, State Territory and Local Governments must ensure that available information on flood risk in their communities is accessible to the public, and
- State, Territory and Local Governments must be implementing and themselves complying with land use planning and building controls in a manner that ensures they are not creating areas of future flood risk.

2.17 As part of this process the COAG Report identified the desired role and responsibility of the insurance industry as being

Insurers have a responsibility to offer effective cover for natural disasters encompassing all hazards for households and businesses at fair and competitive premiums.

In particular the COAG Report noted that normal household insurance should include coverage for all forms of ‘water damage’ and other natural disasters, so avoiding definitional problems, ‘cherry-picking’, complexity, and disputes. The COAG Report further noted that premiums would not need to reflect flood risk, except in areas at high risk of frequent flooding, where a loading or excess could be applied as is the case for areas of high household property crime.

The Insurance Contracts Act

2.18 The *Insurance Contracts Act 1984*, as amended in 2007, broadly seeks to provide a fair balance between the interests of insurers, insureds and other members of the public. Section 35 of the Insurance Contracts Act broadly provides that *standard cover*, being the minimum level of cover for prescribed events, will be deemed to be included in certain

classes of insurance policy, including home buildings insurance and home contents insurance (other than cover notes and renewals). The *standard cover* terms and conditions are set out in the *Insurance Contracts Regulations 1985*, which provide that standard cover in respect of home contents insurance includes loss that is:

... caused by or results from - ... storm, tempest, flood, the action of the sea, high water, tsunami, erosion or landslide or subsidence ...

2.19 Under the Insurance Contracts Act if an insurer seeks to limit or exclude its liability in respect of the standard cover, including provision for flood damage, then the insurer must prove that:

- it clearly informed the consumer of the limitation or exclusion in writing before the contract was entered into; or
- the consumer knew of the limitation or exclusion; or
- a reasonable consumer in the circumstances could be expected to have known of the limitation or exclusion.

3. The application for authorisation

- 3.1 The Insurance Council seeks authorisation of an agreement between its members to adopt, on a voluntary basis, a common definition of “inland flood”.
- 3.2 The arrangement potentially raises concerns under the anti-competitive conduct provisions of the Act. Consequently, the Insurance Council has lodged the application for authorisation with the ACCC.

The proposed definition of “inland flood”

- 3.3 The Insurance Council is proposing a common definition of the term “inland flood”, which is aimed to act as a reference point for the industry, rather than a minimum or maximum standard. The definition of “inland flood” proposed by the Insurance Council is:

Inland Flood is the covering of land that is not normally under water by:

- *water that overflows or escapes from a naturally occurring or man made inland watercourse (such as a river, creek, canal or storm water channel) or a water pool (such as a lake, pond or dam), whether it is in its original state or it has been modified; or*
- *water released from a dam whether it be accidentally released or intentionally released to control, mitigate, regulate, or otherwise respond to excess water, or*
- *water that cannot drain or run off as a result of water that is overflowing or escaping from an inland watercourse or water pool preventing the escape of water.*⁷

- 3.4 The Insurance Council submits that this proposed definition is the result of comprehensive consultation of its members, and will be available for voluntary adoption by members.

Implementation of the proposed definition

- 3.5 As part of the implementation of the proposed definition, the Insurance Council proposes to conduct a “complementary communications campaign” likely to be carried out with the National Flood Advisory Group, which is “designed to raise consumer awareness of the new voluntary common definition.”⁸

Other parties

- 3.6 Under section 88(6) of the Act, any authorisation granted by the ACCC is automatically extended to cover any person named in the authorisation as being a party or proposed party to the conduct. The Insurance Council has sought authorisation for both its present and future members.

⁷ Insurance Council, Submission in support of application for authorisation A91086, 20 March 2008 at page 8.

⁸ Ibid.

4. Submissions received by the ACCC

- 4.1 The Insurance Council provided a supporting submission with its application for authorisation and has also responded to the submissions received from interested parties.
- 4.2 The ACCC sought submissions from around 20 interested parties potentially affected by the application, including consumer organisations, insurance brokers, and relevant government departments. The ACCC received public submissions from:
- the National Insurance Brokers Association; and
 - the Australian Securities and Investments Commission.
- 4.3 Following the release of the draft determination on 3 July 2008 the ACCC sought submissions from interested parties and the Insurance Council commenting upon the conclusions reached by the ACCC in the draft determination. The ACCC received public submissions from;
- the Australian Securities and Investments Commission;
 - the National Insurance Brokers Association;
 - Central Queensland Community Legal Service;
 - the Consumer Action Law Centre;
 - the Consumers' Federation of Australia;
 - the Insurance Law Service;
 - the Legal Aid Commission of New South Wales;
 - Legal Aid Queensland;
 - Mackay Regional Community Legal Centre;
 - Townsville Community Legal Service; and
 - the West Heidelberg Community Legal Service.
- 4.4 The ACCC also convened a pre decision conference in relation to the draft determination on 4 August 2008. A record of the matters discussed at the pre decision conference is available from the ACCC's public register.
- 4.5 The views of the Insurance Council and interested parties are outlined in the ACCC's evaluation of the arrangement in Chapter 6 of this determination. Copies of public submissions are available from the ACCC website (www.accc.gov.au) by following the 'Public Registers' and 'Authorisations Public Registers' links.

5. The net public benefit test

- 5.1 The ACCC may only grant authorisation where the relevant test in section 90 of the Act is satisfied.

Application A91086

- 5.2 The Insurance Council lodged application for authorisation A91086 under section 88(1) of the Act to make and give effect to a contract or arrangement, or arrive at an understanding, a provision of which would have the purpose, or would have or might have the effect, of substantially lessening competition within the meaning of section 45 of the Act. The relevant test for this application is found in section 90(6) of the Act.
- 5.3 In respect of the making of and giving effect to the arrangements, section 90(6) of the Act states that the ACCC shall not authorise a provision of a proposed contract, arrangement or understanding, other than an exclusionary provision, unless it is satisfied in all the circumstances that:
- the provision of the proposed contract, arrangement or understanding would result, or be likely to result, in a benefit to the public; and
 - this benefit would outweigh the detriment to the public constituted by any lessening of competition that would result, or be likely to result, if the proposed contract or arrangement was made and the provision concerned was given effect to.

Application of the tests

- 5.4 The Tribunal has stated that the test under section 90(6) is limited to a consideration of those detriments arising from a lessening of competition.⁹
- 5.5 However, the Tribunal has previously stated that regarding the test under section 90(6):
- [the] fact that the only public detriment to be taken into account is lessening of competition does not mean that other detriments are not to be weighed in the balance when a judgment is being made. Something relied upon as a benefit may have a beneficial, and also a detrimental, effect on society. Such detrimental effect as it has must be considered in order to determine the extent of its beneficial effect.¹⁰
- 5.6 Consequently, when applying the test under section 90(6), the ACCC can take most, if not all, detriments likely to result from the relevant conduct into account either by looking at the detriment side of the equation or when assessing the extent of the benefits.

⁹ *Australian Association of Pathology Practices Incorporated* [2004] ACompT 4; 7 April 2004. This view was supported in *VFF Chicken Meat Growers' Boycott Authorisation* [2006] ACompT9 at paragraph 67.

¹⁰ *Re Association of Consulting Engineers, Australia* (1981) ATPR 40-2-2 at 42788. See also: *Media Council case* (1978) ATPR 40-058 at 17606; and *Application of Southern Cross Beverages Pty. Ltd., Cadbury Schweppes Pty Ltd and Amatil Ltd for review* (1981) ATPR 40-200 at 42,763, 42766.

Definition of public benefit and public detriment

5.7 Public benefit is not defined in the Act. However, the Tribunal has stated that the term should be given its widest possible meaning. In particular, it includes:

...anything of value to the community generally, any contribution to the aims pursued by society including as one of its principle elements ... the achievement of the economic goals of efficiency and progress.¹¹

5.8 Public detriment is also not defined in the Act but the Tribunal has given the concept a wide ambit, including:

...any impairment to the community generally, any harm or damage to the aims pursued by the society including as one of its principal elements the achievement of the goal of economic efficiency.¹²

Future with-and-without test

5.9 The ACCC applies the ‘future with-and-without test’ established by the Tribunal to identify and weigh the public benefit and public detriment generated by arrangements for which authorisation has been sought.¹³

5.10 Under this test, the ACCC compares the public benefit and anti-competitive detriment generated by arrangements in the future if the authorisation is granted with those generated if the authorisation is not granted. This requires the ACCC to predict how the relevant markets will react if authorisation is not granted. This prediction is referred to as the ‘counterfactual’.

Length of authorisation

5.11 The ACCC can grant authorisation for a limited period of time.¹⁴

Future and other parties

5.12 Applications to make or give effect to contracts, arrangements or understandings that might substantially lessen competition or constitute exclusionary provisions may be expressed to extend to:

- persons who become party to the contract, arrangement or understanding at some time in the future¹⁵
- persons named in the authorisation as being a party or a proposed party to the contract, arrangement or understanding.¹⁶

¹¹ *Re 7-Eleven Stores* (1994) ATPR 41-357 at 42,677. See also *Queensland Co-operative Milling Association Ltd* (1976) ATPR 40-012 at 17,242.

¹² *Re 7-Eleven Stores* (1994) ATPR 41-357 at 42,683.

¹³ *Australian Performing Rights Association* (1999) ATPR 41-701 at 42,936. See also for example: *Australian Association of Pathology Practices Incorporated* (2004) ATPR 41-985 at 48,556; *Re Media Council of Australia (No.2)* (1987) ATPR 40-774 at 48,419.

¹⁴ Section 91(1).

6. ACCC evaluation

6.1 The ACCC's evaluation of the proposal by the Insurance Council for the voluntary adoption of a common definition of 'inland flood' is in accordance with the net public benefit test outlined in Chapter 5 of this determination. As required by the test, it is necessary for the ACCC to assess the likely public benefits and detriments flowing from the proposed arrangement.

6.2 Key issues for consideration raised during the course of the ACCC's consultation process were:

- the potential for a standard definition to promote greater recognition and understanding of flood insurance amongst consumers
- the potential for a standard definition to result in the simplification and harmonisation of complex contractual terms dealing with flood insurance
- concerns that the Insurance Council's proposal may restrict competition between insurers in the provision of flood cover
- concerns that the Insurance Council's proposal may reduce the current level of product differentiation between insurers in relation to flood cover
- concerns as to the effectiveness of the Insurance Council's proposed communications campaign
- concerns about the terminology put forward by the Insurance Council, in particular that the proposed definition introduces new terminology, expands established concepts and seeks to diminish the doctrine of proximate cause
- concerns that the Insurance Council's proposed common definition, by potentially increasing consumer confusion, may inhibit the ability of consumers to make informed choices leading to an increased risk that consumers may obtain cover which is inappropriate for their needs
- concerns that, in the absence of strong industry support for a move to greater harmonisation of contractual terms dealing with flood insurance, the Insurance Council's proposal would deliver limited benefits to consumers.

These issues are discussed in greater detail below, including taking into account the submissions made by the Insurance Council and interested parties both before and following the draft determination.

Having had regard to the information provided to it the ACCC can not be satisfied that the proposed common definition is likely to result in a public benefit that will outweigh its likely public detriment.

The ACCC has therefore decided to **deny** authorisation to application A91086.

¹⁵ Section 88(10).

¹⁶ Section 88(6).

The market

- 6.3 The first step in assessing the effect of the conduct for which authorisation is sought is to consider the relevant market(s) affected by that conduct.
- 6.4 The Insurance Council submits the relevant area of competition is the market for the provision of general insurance in Australia. 'General insurance' includes: domestic motor; home; CTP; accident and travel; fire and industrial special risks; commercial motor; public and product liability; and marine. As a general observation the Insurance Council notes that most insurers have various worded exclusions for flood cover. In circumstances where flood cover is offered it is generally provided as an 'add-on' or optional extra rather than a standard inclusion.
- 6.5 In making this submission the Insurance Council notes that in its view a company supplying one type of insurance can easily diversify into other types of insurance and that all types of insurance are able to be moved from one insurer to another very easily. In respect of product diversification the Insurance Council notes that a holder of a general insurance licence can write any type of insurance. The Insurance Council considers that the proposal may make it more attractive for insurers to offer commercial, ISR or home and contents insurance which could potentially cover flood damage.¹⁷
- 6.6 In respect of geographic constraints the Insurance Council considers that the market for general insurance is likely to be national, noting that most insurers are represented in each State and that barriers to cross-State expansion are low.
- 6.7 As noted in Chapter 2 of this determination, in respect of market participation, statistics published by APRA¹⁸ note that over the 2006/2007 financial year general insurance products were offered by 111 direct insurers, earning gross premium revenue of \$28.0 billion. APRA notes that the market concentration in premium revenue from personal classes of business has grown sharply over the year ended June 2007. The top three general insurance groups accounted for 83% of gross premium revenue from personal business, 5% higher than in the previous twelve month period. The top five groups accounted for 91% of gross premium revenue from personal business, 2% higher than in the previous twelve month period.
- 6.8 In its draft determination the ACCC considered that, for the purpose of assessing the Insurance Council's proposal, the definition of 'inland flood' is of particular relevance to the supply of general insurance products. The ACCC noted that general insurance products are offered by a broad range of insurance providers participating in the insurance market on a national or multi-state basis. The ACCC concluded that, for the purposes of its assessment of the Insurance Council's proposal, it was not necessary to further identify the relevant market features.
- 6.9 The ACCC did not receive submissions commenting upon its proposed assessment of the market features relevant to the Insurance Council's proposal. Accordingly the

¹⁷ Insurance Council, Submission in support of application for authorisation A91086, 20 March 2008 at pages 10 - 11

¹⁸ *Statistics - Half Yearly General Insurance Bulletin*, APRA, June 2007 (Revised 25 February 2008)

ACCC adopts the assessment of the relevant market features as set out in the draft determination.

The counterfactual

- 6.10 As noted in Chapter 5 of this determination, in order to identify and measure the public benefit and public detriment generated by conduct, the ACCC applies the ‘future with-and-without test’.
- 6.11 The Insurance Council has submitted that if authorisation is not granted and the common definition of inland flood is not adopted, the likelihood is that the position will remain as it is currently. In the Insurance Council’s view it is likely that consumer confusion around flood cover would continue in this environment.
- 6.12 In particular the Insurance Council has noted that understanding the distinction between damage caused by storm and damage caused by flood is important to enable consumers to appreciate the true extent of their insurance cover, at the time they are purchasing it. The Insurance Council considers that variable definitions for common words (particularly the word ‘flood’) and technical meanings for otherwise commonly used words (such as ‘watercourses’) are not readily understood by consumers and often come to the forefront when claims are made after major flooding. The Insurance Council considers that the proposed common definition for inland flood will act as a guide to industry and will assist consumers in comparing the different types of flood cover offered by insurers.
- 6.13 Following a series of significant flooding events in recent years, there has been an increased focus on consumer understanding of insurance for flood damage and an increased focus on the availability of this cover. As noted at paragraphs 2.16 to 2.17, the recommendations of the COAG Report have sought to create an environment in which household insurance includes coverage for all forms of ‘water damage’ and other natural disasters. The COAG Report noted that in this environment insurance premiums would not need to reflect flood risk, except in areas at high risk of frequent flooding, where a loading or excess could be applied as is the case for areas of high household property crime.
- 6.14 The recommendations of the COAG Report were endorsed in principle by COAG in December 2003. Since this time the Disaster Mitigation Australia Package has been implemented to give effect to the recommendations of the COAG Report. The Insurance Council has also noted these developments.¹⁹
- 6.15 The Disaster Mitigation Australia Package is intended to deliver improvements in flood mitigation measures and improvements in the accuracy of historical flood risk information. These measures are independent of the Insurance Council’s proposed common definition and the ACCC expects that they will lead to improvements in the availability of insurance for flood damage. In *Current Issues Brief – Residential Flood Insurance*, the Insurance Council has itself supported this conclusion noting that flood

¹⁹ Insurance Council, Submission in support of application for authorisation A91086, 20 March 2008 at page 7.

insurance is likely to be more widely available when the risk of flooding is reduced to an acceptable level through mitigation measures.²⁰

- 6.16 The counterfactual must be considered in the broader context of the reform agenda being undertaken by governments and the insurance industry. In its draft determination the ACCC considered that if authorisation were not to be granted to the Insurance Council's common definition proposal the broader reform agenda would continue to be progressed and that this would of itself lead to a reduction in the level of consumer confusion in respect of flood cover.
- 6.17 The ACCC did not receive submissions specifically commenting upon the counterfactual against which it proposed to assess the Insurance Council's application. Having assessed the materials provided to it the ACCC affirms the counterfactual proposed in the draft determination.

Public detriment

- 6.18 The Insurance Council believes the proposed common definition will not lead to a lessening of competition and will not lead to any anti-competitive detriment for the following reasons:
- the proposal should not have the effect of limiting the availability of flood cover and may in fact stimulate interest in providing cover;
 - insurers are free to modify the common definition to suit their risk appetite;
 - insurers are unlikely to gravitate towards retaining the common definition as a minimum standard because competitive forces will continue to influence the price and quality of insurance premiums; and
 - it is likely that insurers will continue to compete vigorously by product differentiation.

Potential anti-competitive detriment resulting from the proposed common definition

- 6.19 The Insurance Council has noted that policy descriptions of 'flood' differ widely between insurers. It has however noted that, for insurance purposes, flood damage generally refers to the inundation of a property by water which overflows from a natural watercourse, while storm and tempest damage refers to the inundation of a property by water as the result of a storm.²¹
- 6.20 The Insurance Council notes that while most home and contents policies cover storm damage, being the inundation of a property by water as the result of a storm, this coverage is commonly subject to a number of exclusions, being:
- tidal inundation caused by the action of the sea, erosion landslide or tsunami; or

²⁰ *Current Issues Brief – Residential Flood Insurance*, Insurance Council of Australia, <http://www.insurancecouncil.com.au/Residential-Flood-Insurance/default.aspx>

²¹ Insurance Council, Submission in support of application for authorisation A91086, 20 March 2008 at page 6.

- damage caused by mingled waters from a storm and the overflow of a natural watercourse; or
 - damage the proximate cause of which is another phenomenon, such as earth movement, even though this may itself have been caused by water from a storm.
- 6.21 In the context of consumer confusion, the June 2000 report *Consumer understanding of flood insurance* published by the ASIC noted that most insurance policies do not cover:
- damage to a property caused by the inundation of water flowing from a natural watercourse; or
 - damage where the property is inundated by mingled waters from the storm and from the overflow of a natural watercourse (unless most of the damage is caused by stormwater); or
 - damage where the proximate cause of the damage is another phenomenon, such as earth movement, even though this may itself have been caused by water from a storm.²²
- 6.22 In submissions provided prior to the release of the ACCC's draft determination the ASIC and the NIBA noted that the proposed common definition is broader than definitions of flood damage currently applied by insurers. Particular focus was given to:
- the inclusion of water overflowing or escaping from man made watercourses, including stormwater channels; and
 - the inclusion of water which cannot drain or run off as a result of water that is overflowing or escaping from an inland watercourse or water pool preventing the escape of water.
- 6.23 Further concerns about the breadth of the proposed common definition were expressed in submissions received following the draft determination by the Consumer Law Action Centre, the Central Queensland Community Legal Service, the Consumers' Federation of Australia, the Insurance Law Service, the Legal Aid Commission of New South Wales, Legal Aid Queensland, the Mackay Regional Community Legal Centre, the Townsville Community Legal Service and the West Heidelberg Community Legal Service (the joint consumer submission).
- 6.24 The ACCC notes that the ASIC and the NIBA have submitted that the effect on consumers of the broader common definition will depend upon whether it is adopted by insurers to define cover offered or to define the terms of an exclusion. The link between the potential effect on consumers and the adoption of the common definition as either an inclusion or exclusion was acknowledged by the Insurance Council in submissions provided prior to the release of the ACCC's draft determination.²³

²² *Consumer understanding of flood insurance*, Australian Securities and Investments Commission, June 2000, at page 7

²³ Insurance Council, Submission in response to interested parties, 15 May 2008 at pages 1 - 2.

- 6.25 The ASIC, the NIBA and the consumer representatives have each argued that, in light of current practices, it is more likely that the common definition will be adopted by insurers to define an exclusion under a policy.
- 6.26 The ASIC and the NIBA have further argued that the adoption of the broader common definition as an exclusion will result in a reduction in flood cover offered to consumers. These concerns have been supported in submissions received from the consumer representatives. In their joint submissions the consumer representatives expressed concern that the Insurance Council's proposal would have a disproportionate impact on low income and disadvantaged consumers, submitting that the proposed definition was likely to be adopted by low cost insurers as an exclusion. The consumer representatives argued that this would lead to an increase in the rejection of claims made by price sensitive consumers.
- 6.27 Particular concerns have been expressed that the inclusion in the proposed common definition of water overflowing or escaping from man made watercourses, including stormwater channels will lead to a reduction in cover provided to consumers.
- 6.28 In submissions provided prior to the release of the draft determination the Insurance Council argued that the inclusion of storm water channels was not intended to eliminate cover where it currently exists for inundation caused by overflow from local stormwater gutters or drains, but to allow for the inclusion of the larger stormwater channels that are in effect concreted rivers and creeks. The Insurance Council submitted that the treatment of such domesticated culverts under insurance policies has lead to consumer confusion in the past.²⁴
- 6.29 In responding to this issue the consumer representatives argued that the Insurance Council's submissions that stormwater channels are domesticated natural watercourses had not been supported by factual evidence and was in their view incorrect. The consumer representatives were further concerned that the expansion of the definition of flood beyond its ordinary meaning to include man made watercourses would of itself result in consumer confusion and public detriment.
- 6.30 The ACCC's draft determination invited further information from the Insurance Council and interested parties analysing the differences in cover offered under current policies and that which may be offered under the proposed common definition so that this issue could be considered further. The ACCC also invited further information from the Insurance Council on the likelihood of the common definition being adopted as either an inclusion or an exclusion.
- 6.31 The Insurance Council has not however provided submissions directly responding to these issues. It has however noted that it will not be offering guidance to members on the use of the common definition as either an inclusion or an exclusion, reiterating its earlier submissions that the adoption or otherwise of the common definition is a matter for individual member companies in a competitive market. The Insurance Council notes that the working group of member companies who drafted the wording constructed the definition as an inclusionary statement and has reiterated that the primary purpose of the proposal is not to limit risk but to serve as a benchmark and a

²⁴ Ibid.

common point of reference that can be used by consumers to compare different types of flood cover.

Conclusion

- 6.32 The ACCC notes the advice of the Insurance Council and interested parties that current policy descriptions of ‘flood’ differ widely between insurers. It follows that the adoption of a common definition will result in some variations in the level of cover provided to consumers’ vis-à-vis current arrangements.
- 6.33 The ACCC considers that the proposed common definition has the potential to restrict competition between insurers in the provision of flood cover and has the potential to reduce the current level of product differentiation between insurers in relation to flood cover. The potential for the proposed common definition to result in increased levels of consumer confusion is considered further in the ACCC’s analysis of public benefits.

Public benefit

- 6.34 The Insurance Council submits that the proposed common definition will deliver public benefits, including:
- functioning as one element within the broader government and industry partnered agenda to improve consumer understanding of flood insurance
 - responding to consumer concerns
 - increasing consumer clarity about the insurance products available
 - it will provide a benchmark for competitive comparison by consumers when they are looking to purchase insurance
 - in association with the consumer education campaign, it will heighten consumer awareness of the need to consider whether or not they should acquire flood cover at the point of purchase rather than after they have suffered from a catastrophic event
 - reduces the stress, delay and inconvenience to consumers of disputes with insurers as to the cause of water damage, as over time consumers become more familiar with the concepts
 - in the longer term, it may lead to greater consistency of legal interpretation and certainty in relation to making claims
 - providing the basis for a broad public education campaign to raise consumer awareness of the extent of coverage available in flood insurance policies and
 - helping to address some of the widespread concerns identified regarding the provision of flood insurance services to the community.

- 6.35 Having considered the materials provided to it, the ACCC proposes to evaluate
- the extent to which the common definition will promote recognition and understanding of flood insurance by consumers; and
 - the extent to which the common definition will improve the consistency of contractual terms dealing with flood insurance.

Promoting consumer recognition and understanding of flood insurance

- 6.36 As noted the Insurance Council has submitted that the common definition will reduce consumer confusion in respect of flood cover. The Insurance Council considers that the common definition will do this by creating a mental picture to assist consumers in separating water damage associated with inland flooding from water damage associated with ocean events. The Insurance Council notes that the definition removes the confusing term of ‘riverine’ which suggests a natural rather than manmade watercourse – the proposed common definition does not distinguish between water escaping from a natural or a man-made watercourse.
- 6.37 The Insurance Council considers that the common definition will provide a benchmark that consumers can use to differentiate between insurance products in circumstances where no such benchmark currently exists.
- 6.38 The ASIC report *Consumer understanding of flood insurance* identified three policy distinctions which cause the most confusion for consumers, being that most insurance policies do not cover:
- damage to a property caused by the inundation of water flowing from a natural watercourse; or
 - damage where the property is inundated by mingled waters from the storm and from the overflow of a natural watercourse (unless most of the damage is caused by stormwater); or
 - damage where the proximate cause of the damage is another phenomenon, such as earth movement, even though this may itself have been caused by water from a storm.²⁵
- 6.39 The COAG report noted that the exclusion of riverine flooding from insurance policies is a problem for most consumers who assume they are covered or do not understand the fine print of their policies. For those who are affected by water damage, whether from a storm, urban drainage overflow, flash flooding or riverine flooding, it gives rise to disputes about what is, and what is not, covered.²⁶
- 6.40 In their reports, COAG and the ASIC each noted that consumer understanding of insurance policies would benefit from clear and consistent terminology in respect of

²⁵ *Consumer understanding of flood insurance*, Australian Securities and Investments Commission, June 2000, at page 7.

²⁶ *Natural Disasters in Australia Reforming mitigation, relief and recovery arrangements*, Council of Australian Governments, August 2002, at page 77.

flood, storm and rain water.²⁷ These views have been supported by the submissions of the consumer representatives.

- 6.41 In its submissions the Insurance Council has identified its intention to conduct a broad public education campaign to raise awareness of the extent of coverage available in flood insurance policies. The Insurance Council has noted that the campaign will include a number of key messages about the risk and cost of flooding; the terms of the common definition; and examples of flood activity covered by the common definition. The Insurance Council has proposed that the campaign be predominantly web delivered – and has identified its intention to develop a dedicated web-page which may be accessed via member websites. This page will include a three minute communications video (which may also be employed at community briefing sessions). The Insurance Council has submitted that this is a logical and reasonable approach in an environment in which consumers are increasingly browsing for insurance products on line. The Insurance Council will develop and release a flyer on the proposed flood definition and its application that will be made available to member companies to use as part of any direct marketing campaign they choose to undertake. Consumers will be encouraged to contact their insurer for information about their own policy.
- 6.42 In its submission following the release of the draft determination the ASIC has noted that based upon its experience in promoting financial literacy the effectiveness of educational messages is increased where those messages are appropriately targeted and, if possible, personalised. The ASIC submits that a campaign which requires consumers to take the initiative and seek further information from the Insurance Council’s website does not satisfy these criteria when compared to messages directed to consumers in flood prone areas. The ASIC has also noted that the Insurance Council’s proposed education campaign would be improved if it provided examples of flood activity falling outside the scope of the common definition.
- 6.43 Submissions provided by the consumer representatives have expressed concern about the Insurance Council’s capacity to conduct an effective education campaign, submitting that the Insurance Council’s current website lacks content specifically aimed at informing and educating consumers and that the Insurance Council’s previous history of communications with consumers demonstrates significant problems. The consumer representatives have argued that the communications campaign should be supervised by and be accountable to the ASIC with its objectives clearly stated in advance.
- 6.44 In responding to this concern the Insurance Council has reiterated its earlier submissions that an upgrade to the Insurance Council’s website is to be undertaken to facilitate the delivery of consumer information on flood, including access to video explanations of the definition and information about broader issues such as flood mapping and links to preparatory guides for consumers facing imminent flood risks.

²⁷ *Consumer understanding of flood insurance*, Australian Securities and Investments Commission, June 2000, at page 4; *Natural Disasters in Australia Reforming mitigation, relief and recovery arrangements*, Council of Australian Governments, August 2002, at page 80.

Conclusion

- 6.45 Noting these areas of concern, the ACCC considers that initiatives which assist consumers in understanding flood insurance are of benefit to the public. The ACCC considers that for the common definition to contribute to the attainment of this benefit it must be widely recognised and understood by consumers.
- 6.46 The ACCC considers that an effective and targeted communications campaign will improve consumer recognition and understanding of flood insurance. The inclusion of the common definition in such a campaign will support the informed comparison of insurance policies by consumers, in part by allowing them to applying the common definition as a benchmark. Proposals such as a standard definition can promote improvements in the appropriateness of cover obtained by consumers by providing them with the resources necessary to allow them to make better informed decisions.
- 6.47 In its draft determination the ACCC expressed concern that the effectiveness of the communications campaign in the form initially proposed by the Insurance Council was likely to be limited. The ACCC also noted concern that whilst the communications campaign was integral to the public benefits arising from the common definition proposal, the communications campaign was not an element of the arrangement for which authorisation had been sought. Given these circumstances the ACCC considered that the uncertainty attached to this potential public benefit was increased.
- 6.48 While noting the Insurance Council's submissions on this matter, the ACCC considers that the concerns set out in the draft determination remain such the likelihood of this public benefit arising is too uncertain for the ACCC to be able to place significant weight on it.

Improving the consistency of contractual terms dealing with flood insurance

- 6.49 The Insurance Council has submitted that the necessity for an industry-wide consensus on flood insurance has been identified in the recommendations of the COAG Report and the ASIC's report *Consumer understanding of flood insurance*.
- 6.50 The COAG Report recommended, in part, that the insurance industry take active steps to develop a single national definition of natural hazards, including water damage, to be offered by all insurers. In its report the ASIC noted that:
- Where possible insurers should simplify and harmonise the drafting of insurance policies so that the availability or exclusion of flood insurance under house and contents insurance policies is made clear.²⁸*
- 6.51 Submissions received from the consumer representatives and the NIBA have also expressed support for the development of a common definition by the insurance industry. The consumer representatives have noted that potential public benefits of the standardisation of the definition of 'flood' are a reduction in consumer confusion, more informed decision making and fairer coverage for consumers with flood exclusions in their policy.

²⁸ *Consumer understanding of flood insurance*, Australian Securities and Investments Commission, June 2000, at page 4.

- 6.52 The ACCC considers that, in relation to flood insurance, the simplification and harmonisation of complex contractual terms is likely to result in public benefit by improving the consistency of contractual terms dealing with flood insurance. As noted at paras 2.18 – 2.19 of this determination the *Insurance Contracts Regulations* provide that *standard cover* in respect of home and contents insurance includes loss that is caused by or results from flood. The *Insurance Contracts Regulations 1985* and *Insurance Contracts Act 1984* do not however provide a definition of ‘flood’. This has led to the development of a range of policy descriptions of ‘flood’ by insurers on an individual basis.
- 6.53 Submissions made by the consumer representatives, ASIC and NIBA have raised strong concerns about the specific terminology proposed by the Insurance Council’s common definition.

For ease of reference the common definition proposed by the Insurance Council is reproduced below.

Inland Flood is the covering of land that is not normally under water by:

- *water that overflows or escapes from a naturally occurring or man made inland watercourse (such as a river, creek, canal or storm water channel) or a water pool (such as a lake, pond or dam), whether it is in its original state or it has been modified; or*
- *water released from a dam whether it be accidentally released or intentionally released to control, mitigate, regulate, or otherwise respond to excess water, or*

*water that cannot drain or run off as a result of water that is overflowing or escaping from an inland watercourse or water pool preventing the escape of water.*²⁹

- 6.54 The concerns raised by the consumer representatives, the ASIC and the NIBA can be summarised as:

- concern that the use of the expression ‘inland’ is unhelpful and may lead to increased consumer confusion as to the application of the proposed common definition to coastal communities;
- concern that the use of the term ‘water pool’ will increase consumer confusion as the ordinary meaning of water pool is not one usually associated with flood;
- concern that inclusion of man made watercourses would of itself result in consumer confusion and public detriment;
- concern that the definition seeks to diminish the doctrine of proximate cause, potentially exposing consumers to loss arising from the negligent acts of third parties; and
- concern that the third limb of the proposed definition is likely to result in the denial of cover in a range of circumstances that would ordinarily be covered by a general insurance policy – examples include damage arising from excessive stormwater where that water is prevented from escaping due to rising flood waters.

²⁹ Insurance Council, Submission in support of application for authorisation A91086, 20 March 2008 at page 8.

- 6.55 In their joint submission the consumer representatives have noted their willingness to work with the Insurance Council to develop a standard definition for flood that provides legal certainty, public clarity and a fairer outcome for consumers.
- 6.56 In responding to the concerns raised by the consumer representatives, the ASIC and the NIBA, the Insurance Council has noted that there is a degree of uncertainty inherent in any new definition. The Insurance Council has argued that this is an issue inherent in any change to policy terms and is not a sufficient reason to refrain from implementing a benchmark definition.
- 6.57 In submissions provided prior to the release of the draft determination, the ASIC and the NIBA argued that insurers should not be allowed to adopt the definition in part as this would defeat the intention of giving the phrase a distinct and readily recognisable meaning. The NIBA also submitted that insurers who do not adopt the common definition (in whole) should disclose to consumers in simple and concise terms the differences between their policy and the common definition.
- 6.58 In submissions provided prior to the draft determination the Insurance Council disagreed with these views, submitting that insurers must be free to develop their insurance policies in a manner that suits their business. The Insurance Council also submitted that individual insurers maintaining alternate definitions to the proposed common definition were unlikely to diminish the effectiveness of the common definition proposal.³⁰
- 6.59 The Insurance Council has also not identified the extent to which it expects its members to take-up the proposed common definition. The Insurance Council has noted recent trends in the provision of flood insurance which has seen a growth in residential policies provided by members which include flood cover – from approximately 8% in late 2006 to approximately 32% at the present time. The Insurance Council has noted that it expects this trend to continue and that in this environment the common definition will provide a useful benchmark for consumers.
- 6.60 In this respect the ACCC also notes the recent developments under which certain insurers have elected to introduce flood cover, for example see Zurich³¹ and Suncorp.³² The ACCC notes the recent statements by Zurich indicating that it will not be adopting the Insurance Council’s proposed standard definition.³³ Suncorp has not indicated whether it would amend the definition of flood which it adopted as an inclusion on 1 July 2008.

³⁰ Insurance Council, Submission in response to interested parties, 15 May 2008 at page 2.

³¹ From 8 September 2008 Zurich Financial Services Australia will offer flood cover to commercial customers. For further information see www.zurich.com.au.

³² From 1 July 2008 all home and contents insurance policies offered by Suncorp under its Suncorp and GIO brands will provide cover for all types of flood caused by rain. This cover applies to customers who take out a new home and contents policy from the 1 July 2008 and to all existing customers who insure their home and contents with members of the Suncorp Group. For further information see www.suncorp.com.au and/or www.gio.com.au.

³³ *Zurich moves on flood cover*, Cover Note 1597, Thompson Legal and Regulatory, August 2008.

Conclusion

- 6.61 It is accepted that definitions of ‘flood’ vary between insurers, however in their submissions interested parties and the Insurance Council have sought to identify terms commonly applied by insurers in seeking to define ‘flood’ – in this respect the Insurance Council has noted that, for insurance purposes, flood damage generally refers to the inundation of a property by water which overflows from a natural watercourse.³⁴ The ACCC is concerned that, to the extent that the proposed common definition introduces concepts which lack legal certainty or applies concepts in a manner which may be inconsistent with their common meaning, the Insurance Council’s proposal may have the unintended consequence of increasing consumer confusion and of diminishing the potential benefits to the public of improving the clarity of contractual terms dealing with flood insurance. To the extent that the Insurance Council’s proposed common definition increases consumer confusion, the proposed common definition may inhibit the ability of consumers to make informed choices leading to an increased risk that consumers may obtain cover which is inappropriate for their needs, or obtain cover that is not competitively priced when regard is had to its features.
- 6.62 The ACCC is also concerned that if individual insurers were able to modify the common definition the potential benefit associated with the accessibility of information disclosed to consumers would be significantly reduced. The ACCC notes that the freedom to modify the common definition has the potential to result in greater confusion about the definition of flood because it may become unclear what the standard definition is if in practice there are a number of versions of the standard. In addition, in the absence of strong industry support for a move to greater harmonisation of contractual terms dealing with flood insurance, the ACCC considers that the proposal will deliver limited benefits to consumers.
- 6.63 While noting the Insurance Council’s submissions on this matter, the ACCC considers that the concerns set out in the draft determination remain. In this environment the likelihood of this public benefit arising is too uncertain for the ACCC to be able to place significant weight on it.
- 6.64 The ACCC notes the potential benefits which may arise if insurers were to adopt a policy of disclosing to consumers the differences between their policy and the common definition (a positive disclosure obligation). While this would not address the concerns identified in the COAG Report or by the ASIC, such positive disclosure obligations have the potential to result in improvements in the level of consumer understanding. However as this is not an aspect of the arrangement for which the Insurance Council is seeking authorisation it is not a potential public benefit for which the ACCC may have regard.

Balance of public benefit and detriment

- 6.65 The ACCC may only grant authorisation if it is satisfied that, in all the circumstances, the proposed common definition is likely to result in a public benefit that will outweigh any public detriment.

³⁴ Insurance Council, Submission in support of application for authorisation A91086, 20 March 2008 at page 6.

- 6.66 In the context of applying the net public benefit test at section 90(8)³⁵ of the Act, the Tribunal commented that:
- ... something more than a negligible benefit is required before the power to grant authorisation can be exercised.³⁶
- 6.67 Policy descriptions of ‘flood’ differ widely between insurers – in this environment the adoption of a common definition will result in some variations in the level of cover provided to consumers vis-à-vis current arrangements.
- 6.68 The ACCC considers that the proposed common definition has the potential to restrict competition between insurers in the provision of flood cover and has the potential to reduce the current level of product differentiation between insurers in relation to flood cover.
- 6.69 Balanced against this anti-competitive detriment, the ACCC recognises the potential for a standard definition to promote greater recognition and understanding of flood insurance amongst consumers. A standard definition can promote improvements in the appropriateness of cover obtained by consumers by providing them with the information necessary to allow them to make better informed decisions. Consumer representatives have noted that a standard definition for flood is likely to result in a reduction in consumer confusion, more informed decision making, and fairer coverage for consumers, including better informed pricing decisions.
- 6.70 The ACCC considers that the extent to which the Insurance Council’s proposal is likely to assist in promoting consumer recognition and understanding of flood insurance is largely dependent upon the effectiveness of the Insurance Council’s proposed communications campaign.
- 6.71 Submissions provided to the ACCC have raised concerns about the likely effectiveness of the communications campaign as proposed by the Insurance Council. These submissions have noted that a communications campaign which requires consumers to take the initiative and seek further information from the Insurance Council’s website is unlikely to be effective.
- 6.72 While it notes the Insurance Council’s submissions on this issue, the ACCC considers that the concerns set out in the draft determination remain such the likelihood of this public benefit arising is too uncertain for the ACCC to be able to place significant weight on it.
- 6.73 The ACCC is also concerned that whilst the communications campaign is integral to the public benefits arising from the common definition proposal, the communications campaign is not an element of the arrangement for which authorisation has been sought. In these circumstances the uncertainty attached to this potential public benefit is increased.

³⁵ The test at 90(8) of the Act is in essence that conduct is likely to result in such a benefit to the public that it should be allowed to take place.

³⁶ *Re Application by Michael Jools, President of the NSW Taxi Drivers Association* [2006] ACompT 5 at paragraph 22.

- 6.74 The ACCC considers that, in relation to flood insurance, the simplification and harmonisation of complex contractual terms is likely to result in public benefit by improving the consistency of contractual terms dealing with flood insurance.
- 6.75 However submissions put by the consumer representatives, ASIC and NIBA have raised strong concerns about the terminology proposed by the Insurance Council, arguing that the proposed definition introduces new terminology, expands established concepts and seeks to diminish the doctrine of proximate cause.
- 6.76 In responding to this concern the Insurance Council has noted that there is a degree of uncertainty inherent in any new definition. The Insurance Council has argued that this is an issue inherent in any change to policy terms and is not a sufficient reason to refrain from implementing a benchmark definition.
- 6.77 The ACCC is concerned that, to the extent that the proposed common definition introduces concepts which lack legal certainty or applies concepts in a manner which may be inconsistent with their common meaning, the Insurance Council's proposal may have the unintended consequence of increasing consumer confusion and of diminishing the potential benefits to the public of improving the consistency of contractual terms dealing with flood insurance. To the extent that the Insurance Council's proposed common definition increases consumer confusion, the proposed common definition may inhibit consumers in making informed choices leading to an increased risk that consumers may obtain cover which is inappropriate for their needs.
- 6.78 The ACCC considers that the consistent adoption of the common definition is an important factor in securing the Insurance Council's claimed public benefits. To the extent that the industry modifies the Insurance Council's proposed benchmark the potential public benefits of the proposal are further diminished. In the absence of strong industry support for a move to greater harmonisation of contractual terms dealing with flood insurance, the ACCC considers that the proposal will deliver limited benefits to consumers.
- 6.79 Having considered these factors the ACCC is not satisfied that the proposed common definition is likely to result in a public benefit that will outweigh any public detriment.

Conditions

- 6.80 In its draft determination the ACCC considered that that the net public benefit test may be satisfied following the imposition of a number of conditions intended to provide greater certainty that the proposed common definition would assist consumers in understanding flood insurance and would result in improvements in the consistency of contractual terms dealing with flood insurance.
- 6.81 In its draft determination the ACCC proposed to grant authorisation subject to the following condition(s):

Condition 1

That the Insurance Council undertake a comprehensive and effective consumer education campaign to improve consumer awareness of flood insurance and provide to the ACCC a bi-annual report on the educational activities undertaken and their effectiveness for inclusion on the ACCC's public register.

Condition 2

That the Insurance Council provide a bi-annual report to the ACCC for inclusion on its public register detailing the adoption of the common definition by members, including the number of insurance policies written by members containing the common definition as a term of the contract.

Condition 3

That the members of the Insurance Council adopting the common definition clearly and prominently disclose this to insureds and prospective insureds.

Condition 4

Members of the Insurance Council adopting the common definition in accordance with this authorisation are not permitted to modify the common definition.

- 6.82 The ACCC received submissions from the Insurance Council and interested parties commenting upon the proposed conditions. In its submission the Insurance Council proposed a number of refinements to draft conditions one, two and four and asked that the ACCC reconsider the necessity of imposing draft condition three in light of member obligations under financial services regulations in respect of product disclosure statements.
- 6.83 In their submissions the consumer representatives expressed concern that the ACCC's proposed conditions may have the effect of increasing consumer confusion by promoting an assumption by consumers that the common definition automatically applies to their own policies whether this is the case or not. The consumer representatives noted that this effect would be reduced in an environment in which a common definition in respect of exclusions had been mandated, allowing for competition between insurers in respect of flood inclusions.

Conclusion on the balance of public benefit and detriment

- 6.84 Having considered the materials before it the ACCC is not satisfied that the proposed common definition is likely to result in a public benefit that will outweigh any public detriment.
- 6.85 As noted the ACCC considers that the proposed common definition has the potential to restrict competition between insurers in the provision of flood cover and has the potential to reduce the current level of product differentiation between insurers in relation to flood cover.
- 6.86 Balanced against this, the ACCC and interested parties have recognised the potential for a standard definition to promote a better understanding of flood insurance amongst consumers. A standard definition can promote improvements in the appropriateness of cover obtained by consumers by providing them with the information necessary to allow them to make better informed decisions. The ACCC also considers that, in relation to flood insurance, the simplification and harmonisation of complex contractual terms is likely to result in a benefit to the public by improving the clarity of contractual terms dealing with flood insurance.

- 6.87 However in the circumstances the ACCC can not be satisfied that the Insurance Council's proposal will deliver these benefits to the public. The ACCC is concerned that, to the extent that the proposed common definition introduces concepts which lack legal certainty or applies concepts in a manner which may be inconsistent with their common meaning, the Insurance Council's proposal may have the unintended consequence of increasing consumer confusion and of diminishing the potential public benefits of the proposal.
- 6.88 In its draft determination the ACCC also considered that the Insurance Council's proposal was unlikely to result in a net benefit to the public. At that time the ACCC considered that its concerns could be alleviated through the imposition of conditions such that authorisation could be granted.
- 6.89 In light of the materials now before it the ACCC can no longer be satisfied that the imposition of conditions would alleviate these concerns. In particular the ACCC notes that the potential for the proposed common definition to introduce new concepts and to increase consumer confusion is not a concern which can be addressed by the imposition of conditions.
- 6.90 The ACCC has therefore decided to **deny** authorisation to application A91086.
- 6.91 The ACCC recognises the efforts by Government and industry aimed at improving both the availability of flood insurance and consumer understanding of flood issues. The ACCC also recognises that this is a complex issue and encourages the Insurance Council and its members to continue working with consumer groups and other interested stakeholders.
- 6.92 The ACCC encourages the Insurance Council, its members and interested stakeholders to consider refinements to the proposed common definition which may alleviate the concerns identified by this determination.
- 6.93 The ACCC notes that its decision in this matter does not prevent the insurance industry from seeking authorisation of a revised proposal in the future.

7. Determination

The application

- 7.1 On 20 March 2008 the Insurance Council of Australia lodged application for authorisation A91086 with the Australian Competition and Consumer Commission (the ACCC).
- 7.2 Application A91086 was made using Form B Schedule 1, of the Trade Practices Regulations 1974. The application was made under subsection 88(1) of the Act for an agreement between members (both present and future) of the Insurance Council of Australia Limited to voluntarily adopt a common definition of 'inland flood' for the purposes of provision of flood insurance services to the community.

Inland Flood is the covering of land that is not normally under water by:

- *water that overflows or escapes from a naturally occurring or man made inland watercourse (such as a river, creek, canal or storm water channel) or a water pool (such as a lake, pond or dam), whether it is in its original state or it has been modified; or*
- *water released from a dam whether it be accidentally released or intentionally released to control, mitigate, regulate, or otherwise respond to excess water, or*
- *water that cannot drain or run off as a result of water that is overflowing or escaping from an inland watercourse or water pool preventing the escape of water.*

The net public benefit test

- 7.3 For the reasons outlined in Chapter 6 of this determination the ACCC considers that in all the circumstances the arrangements for which authorisation is sought are **not** likely to result in a public benefit that would outweigh the detriment to the public constituted by any lessening of competition arising from the arrangements.
- 7.4 The ACCC has therefore decided to **deny** authorisation to application A91086.
- 7.5 This determination is made on 3 September 2008. If no application for review of the determination is made to the Australian Competition Tribunal, it will come into force on 26 September 2008.