



Australian Government



Australian
**Small Business and
Family Enterprise**
Ombudsman

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Senator Mehreen Faruqi

Chair, Select Committee on the Impact of Climate Change on Insurance Premiums and Availability
PO Box 6100

Parliament House, Canberra, ACT 2600

via email: climaterisk.insurance.sen@aph.gov.au

Dear Senator Faruqi

Impact of Climate Change of Insurance Premiums and Availability

The Australian Small Business and Family Enterprise Ombudsman (ASBFEO) welcomes the opportunity to provide comments to the Committee's inquiry into the impacts of climate change on insurance premiums and availability.

The purpose of the Australian Small Business and Family Enterprise Ombudsman (ASBFEO) is to contribute to making Australia the best place to start, grow and transform a business. One of our key functions is to advocate for small and family businesses, so that their distinctive needs are considered by the parliament, ministers, departments and regulators. While it is not in the ASBFEO's power to guarantee that every small business will be a success, it is our mission to make sure none fails because they didn't know about something that would help.

Since the 2019 -20 Black Summer bushfires, insurers have paid out more than \$16.8 billion in natural disaster claims from 13 declared catastrophes and 5 significant events, with the 2022 flooding of North East NSW and South East Queensland being the most costly natural disaster in Australian history (adjusted for inflation).¹

The summer of 2023-24 saw several extreme weather events across the east coast, with two declared 'catastrophes' by the ICA, including a cyclone and severe storms and flooding in Queensland. The ICA has released data that show losses from declared catastrophes last summer to have reached close to \$1.6 billion, with the cost of the Christmas storms now exceeding \$1.1 billion.²

Natural disasters can present systemic risks to society, affecting not just to individuals and communities, but also to the economy and infrastructure. For many small businesses operating in regions that are at risk of natural disasters, they are increasingly finding it difficult to find affordable insurance, particularly for insurances that cover commercial property and, in some areas, public liability.

The Intergovernmental Panel on Climate Change's (IPCC) Sixth Assessment Report projects the frequency and duration of fire, rainfall and flooding is expected to continue to increase owing to

¹ Insurance Council of Australia (ICA), Insurance Catastrophe Resilience Report 2022-23, ICA, n.d. p 9

² ICA, *ICA declares weekend storm a 'Significant Event'*, ICA, 10 April 24



climate change.³ As natural disasters increase in frequency and severity, the number of households and businesses impacted will increase resulting in high claim costs that will continue to put upward pressure on insurance premiums.

Access to adequate insurance cover at commercially viable terms is a significant challenge for many of Australia's small businesses. The ASBFEO's *Small Business Natural Disaster Preparedness and Resilience Inquiry Report* found that:

- many businesses cannot secure appropriate insurance at an affordable price
- some businesses are operating uninsured, or significantly underinsured, with excesses that would preclude any claim being made
- insurers are uninterested in the steps individual small and family businesses take to mitigate disaster risk or are dismissive of them.⁴

Further, businesses surveyed by Business NSW consider insurance to be the number one cost pressure over taxes and other charges, energy costs, and wages.⁵ There has been a distinct shift in small business concerns since the end of 2023 in Queensland, which has the largest tourism market in Australia (accounting for 28.2% of national tourism output) and a high exposure to natural disasters.⁶ The relative weight of concern has shifted from staffing, housing and general business costs to the costs of electricity and insurance.⁷

Unlike households that – for various reasons – might choose to be uninsured or underinsured and have options about the level and nature of the risk protection policies they subscribe to, a small business must have insurance covering areas such as public liability. If a small business isn't insured, it cannot engage in trade and commerce. Many small and family businesses are individually doing what's being asked of them but are seeing no benefits to cost and availability of insurance cover.

Noting the present challenges affecting small businesses, we provide the following recommendations for consideration by the committee.

Recommendation 1. The insurance sector should help small business by mapping out pathways to solutions that will mitigate risk, and materially improve accessibility and affordability.

While we recognise that there are multiple factors contributing to increasing insurance premiums (such as the hardening insurance market), significant claims have been made against several natural disasters, and underwriters have seen profits decline. We acknowledge that insurance companies and their representatives do highlight methods by which small businesses can reduce

³ Intergovernmental Panel on Climate Change (IPCC), *Sixth Assessment Report – Regional Fact Sheet – Australia*, IPCC, 2021

⁴ Australian Small Business and Family Enterprise Ombudsman, *Small Business Natural Disaster Preparedness and Resilience Inquiry Report*, 10 November 2022.

⁵ Business NSW, *NSW Business Conditions: A cautious start to 2024*, March 2024, pg15

⁶ Queensland Government, *About the Queensland Economy*, 2024, accessed 4 April 2024.

<https://www.treasury.qld.gov.au/queenslands-economy/about-the-queensland-economy>

⁷ Queensland Small Business Commissioner, *From the Commissioner – February 2024*, 2024



premiums, for example by installing fire alarms and security protection. However, small business stakeholders have informed the ASBFEO that insurance companies have been unwilling to reflect private household climate risk mitigation practices with reduced premiums.⁸

The insurance industry should provide a clearer articulation of what policies cover, what is required by small businesses, and how they can work with the insurance industry to address concerns, can give small businesses the chance to stay in business should help small businesses by mapping out pathways to solutions to give small businesses the chance to stay in business.

The ASBFEO considers that insurers should recognise potential savings from risk-mitigation steps undertaken by their small business customers and share these benefits with them. The Australian Disaster Resilience Knowledge Hub (the Hub) acts as a national open-source platform to support and inform policy and decision making in disaster resilience and is run by the Australian Institute for Disaster Resilience. Policies for how risk mitigation actions should be undertaken by small business customers and how their benefits are recognised and shared, should be clearly communicated to small business customers as part of the information that insurance providers are required to share under the Code.

The Caravan Industry Association of Australia undertook stakeholder engagement and collaboration to examine the insurance landscape in the caravan park industry and present a 5-point strategy to address its current challenges related to affordability and accessibility. This approach used data-driven risk-mitigation measures and analysis to understand the industry's risk profile to answer insurance challenges in the sector.⁹

Recommendation 2. Cyclone Reinsurance Pool (the Pool) should be reviewed to determine whether certain industries are excluded and expanded to cover all declared emergencies, including flood and fire.

In March 2022, the Australian Parliament passed the Treasury Laws Amendment (Cyclone and Flood Damage) Reinsurance Pool Bill 2022 to help insurance companies mitigate risk for cyclone related damage, backed by a \$10 billion Government reinsurance guarantee. While the Pool insures both commercial and non-commercial products, we draw attention to the maximum sum of \$5 million allowable for insurance for small business property policies to be covered by the Pool.

We consider that \$5 million is not sufficient to meet the needs of many small businesses. This restrictive limit risks small businesses falling outside the Pool's coverage and may lead to an increase in underinsurance throughout the sector. While the Pool's objective is to lower the premiums for insurance, the ACCC's Insurance Monitoring Report 2023 notes that the effects of the Pool were unlikely to be felt at the time of writing.¹⁰ The government should continue to monitor the Pool's effects and investigate whether it should be expanded to cover all declared emergencies, including floods and fires.

⁸ ICA, *Premiums Explained*, ICA, n.d. Accessed 28 June 2024

⁹ Caravan Industry Association of Australia, *Industry Roadmap Insuring Caravan Parks A Strategic Blueprint to Improve Industry Wide Insurance Affordability and Accessibility*, 2023, accessed 4 April 2024.

¹⁰ Australian Competition and Consumer Commission (ACCC), *ACCC Insurance Monitoring Report 2023*, ACCC, 8 December 2023



The Pool covers businesses with an annual turnover of less than \$10 million, however the structure of some franchises and property tenancy agreements may inadvertently exclude them from coverage where the franchisor or landlord is not eligible. The Pool's definitions should be expanded to ensure that small and medium enterprises are not excluded due to their position in a larger corporate structure.

The Joint Select Committee on Northern Australia's *First Report on the Cyclone Reinsurance Pool* notes that while marine insurance will be included in the Pool from 1 July 2023, there is no specific information on the Australian Reinsurance Pool Corporation's (ARPC) website.¹¹ The ARPC should update its fact sheets to ensure that consumers are provided with clear and unambiguous information about what the Pool covers, including vessels and wharf/jetty infrastructure.

Recommendation 3: Support discretionary mutual funds (DMFs) where appropriate.

Our report: *Additional Insights Supporting a Discretionary Mutual Fund for the Amusement, Leisure and Recreation Industry* supported the creation of a DMF to prevent forced business closures, job losses, and a reduction in activity that is important to livelihoods and communities in regional Australia.¹²

A DMF offers insurance like protection where members make financial contributions to a fund which can then make a decision on whether a claim should be paid out. As a DMF does not issue shares, it has no requirement to distribute returns to shareholders and can therefore operate at a lower profit margin.

Crucially, a DMF would be able to impose conditions of entry standards for members and enforce strong risk-management culture and procedures. DMFs are generally operated by directors with strong industry experience and knowledge of the practical options to mitigate risk and can work with industry bodies to facilitate guidance to members.

Recommendation 4. Account for climate risks in land-use planning.

The Climate Council projects approximately 520,940 properties will be categorised as high risk, and uninsurable by 2030, with 80% of the high-risk properties being affected by riverine flooding. Flash flooding and bushfires are the other main hazards contributing to properties becoming uninsurable.¹³ Following catastrophic weather events or other disasters, it is appropriate to give due consideration to whether rebuilding or moving to a new location with a lower risk profile provides the greater value.

The Australian Government should engage with state and local governments and insurance bodies to develop a system of risk levels and ensure that all land released has been analysed for climate risk and high-risk locations are excluded from development locations.

¹¹ Joint Select Committee on Northern Australia, *First Report on the Cyclone Reinsurance Pool*, Joint Select Committee on Northern Australia, March 2023, p 46

¹² Australian Small Business and Family Enterprise Ombudsman (ASBFEO), *Additional Insights Supporting a Discretionary Mutual Fund for the Amusement, Leisure and Recreation Industry*, ASBFEO, 20 January 2023

¹³ Climate Council, *Uninsurable Nation: Australia's most climate-vulnerable places*, Climate Council, 2022, p 2-3



Once appropriately designated a high-disaster risk area, these communities could have access to all or some of the following measures under an agreed, coordinated, multi-government and agency strategy:

- participation in a government-backed reinsurance vehicle (perhaps modelled on the UK Flood Re solution)
- priority for monitoring and mitigation expenditure
- relaxation of matched funding requirements to access support grants
- enhanced disaster planning arrangements to include federal and state participation given these jurisdictions' anticipated role in any disaster response
- pre-deployment of resilience and recovery assets
- priority-critical infrastructure hardening
- interest-free loans for asset protection, property enhancement, and activity/property relocation schemes
- enhanced small and family business preparedness and resilience support
- incentives for business continuity planning and provisioning
- measures to address acute 'moral hazard' issues
- tailored insurance products including 'like for right' coverage
- greater support for the use of local government rating systems to recover investments across the serviceable life of works and asset improve.

Recommendation 5. The Government should commit to hardening critical infrastructure that enhances disaster preparedness and resilience.

Australian Government infrastructure grants should be dependent on 'hardening' critical infrastructure that enhances disaster preparedness and resilience. Where Australian Government funding is requested to support infrastructure development or repair, there must be a commensurate responsibility to ensure critical infrastructure is fit for purpose for any intended disaster management and response function. For example, funding agreements for critical road upgrades should require that verges are cleared sufficiently to allow access or evacuation in the event of an emergency. Similarly, where telecommunications infrastructure is approved and funded (particularly where government support has been provided), arrangements to ensure durability in the face of a natural disaster should be part of funding requirements.

Recommendation 6. Expand the Hazard Insurance Partnership to include overseas reinsurers and specialty insurance companies.

In September 2023, the Assistant Treasurer and Minister for Financial Services, the Hon Stephen Jones MP led Australia's first delegation of Australian Insurers to the UK and Germany to meet with international reinsurance companies. The Reinsurance companies outlined how the risk of floods had driven insurance companies out of Roma, however infrastructure upgrades that downgraded



the risk allowing insurance companies to reassess underwriting businesses in the area.¹⁴ Insights gained from this meeting demonstrate the effectiveness of high-level engagements with international companies in innovating and developing insurance policy options in the face of global climate change.

In February 2023, the inaugural meeting of the Hazard Insurance Partnership (HIP) was held bringing together the National Emergency Management Agency, insurance bodies, the Australian Bureau of Statistics and Australian Climate Service to investigate ways to reduce insurance premiums and strengthen disaster resilience in Australia.¹⁵ While HIP's membership expanded in June 24 to include more members of the insurance community, we consider that a more diverse array of voices would prove beneficial. We recommend that HIP be expanded to include members from international insurers and reinsurers as well as boutique Australian insurance companies to continue to gain insight from insurance innovations.

A 2019 article by reinsurance company Swiss Re notes that a combination of better risk awareness and policy incentives could help make insurance more widely available.¹⁶ The use of data has allowed innovations in insuring climate-based risk and reducing payment times globally. An example of this includes a new type of cover known as 'weather index insurance', relying on data gathered from remote sensing and satellite imagery to create automatic payouts once weather catastrophes reach an index. A 2018 analysis by J Kath et al found that sugar cane farmers in Tully, North Queensland would be better off by \$269.85/ha on average in a year with excessive rainfall.¹⁷

Recommendation 7. The protections given to retail insurance consumers under the General Insurance Code of Practice should also apply to small businesses.

The General Insurance Code of practice in its current form provides limited protections to small business. While the entire Code applies to retail insurance as defined under the Code, this definition does not extend to insurance products that small businesses often use. Instead, as the Australian Financial Complaints Authority (AFCA) notes in its submission, many types of small business insurance products are treated as wholesale insurance under the Code, meaning that small businesses are largely unprotected by Parts 5 to 9 and 11 of the Code.¹⁸

The ASBFEO considers that this divergence in the level of protection given to households and small businesses to be unsatisfactory and arbitrary, given the close similarities and crossovers in the challenges faced by both groups. As with households, most small businesses do not have the in-house expertise to understand complex insurance products, and given other cost pressures, may not have the resources to seek professional assistance regarding their insurance needs. Furthermore, nearly half of outstanding small business debts are secured by residential property,

¹⁴ The Hon Stephen Jones MP, *Address to the Insurance Council of Australia Conference*, The Treasury, 12 October 2023

¹⁵ Senator The Hon Murray Watt, *Landmark partnership to improve disaster insurance*, Australian Government, 2 February 2023

¹⁶ Swiss Re Group, *Confronting the cost of catastrophe*, Swiss Re Group, n.d. accessed 26 June 2024

¹⁷ J Kath, S Mushtaq, R Henry, A Adeyinka, R Stone, *Index insurance benefits agricultural producers exposed to excessive rainfall risk*, *Weather and Climate Extremes*, Volume 22, 2018, Pages 1-9

¹⁸ Australian Financial Complaints Authority (AFCA), *Submission in response to initial consultation paper*, AFCA, June 2024, p. 12; ICA, *General Insurance Code of Practice*, ICA, 5 October 2021, p. 11.



meaning that not only are the challenges that households and small business face similar, the welfare of the two groups is closely tied together.¹⁹

Accordingly, the ASBFEO recommends that the entire Code should apply to small business insurance products. This would mean that small businesses are protected by the same service standards, consumer protections, support for vulnerable consumers and complaints handling processes as are given to Retail Insurance consumers under the Code.

The ASBFEO supports AFCA's suggestion that the definition of a small business under the Code be aligned with the definition in the AFCA Rules (that is, an organisation with fewer than 100 employees).²⁰ This would reduce inconsistency and confusion in the current Code and dispute-resolution arrangements.

Recommendation 8. APRA should review whether its rules for use of Insurance Linked Securities is appropriate to encourage insurance companies to invest in Australia.

Insurance Linked Securities (ILS) are an alternative method for insurers and reinsurers to seek capital by offloading insured risks to the capital market through securitisation. ILS were developed following Hurricane Andrew's devastation of Florida in 1992 as insurers and reinsurers became unwilling (or unable) to continue to offer insurance cover. Catastrophic bonds represent one version of ILS whose performance is driven by natural events allowing them to withstand much of the pressure in the capital markets during the financial crisis.²¹

In August 2023, the Australian Prudential Regulation Authority (APRA) gave a reminder notice to general insurers that the use of Insurance Linked Securities (ILS) are permitted under APRA standard.²² APRA's regulations on ILS use by general insurers should be reviewed and assessed to determine whether they are appropriate to encourage the capital market to invest in Australian Insurance.

If you require any further information, please do not hesitate to contact the ASBFEO Policy and Advocacy team, via email at advocacy@asbfeo.gov.au.

Yours sincerely

The Hon Bruce Billson
Australian Small Business and Family Enterprise Ombudsman

¹⁹ ASBFEO, *Ombudsman helping small business resolve disputes* [media release], ASBFEO, Australian Government, 31 January 2024.

²⁰ AFCA, *Submission in response to initial consultation paper*, AFCA, June 2024, p. 12. Recall that the Australian Small Business and Family Enterprise Act 2015 defines small business as one that in the current financial year: a. Has fewer than 100 employees at that time; b. either: i. its revenue for the previous financial year is \$5,000,000 or less; or ii. if there was no time in the previous financial year when the business was carried on--its revenue for the current year is \$5,000,000 or less.

²¹ Swiss RE Group, *The fundamentals of Insurance Linked Securities*, Swiss Re Group, 7 September 2011, p 7

²² Australian Prudential Regulation Authority (APRA), *APRA's reinsurance requirements and the use of insurance linked securities*, APRA, 3 August 2023