Australian Government

Australian
Small Business and
Family Enterprise
Ombudsman

The Show Must Go On

Is a discretionary mutual fund the solution to the insurance crisis facing Australia's amusement, leisure and recreation sector?

Final Report

6th December 2021

Contents

Spending a day at the show is a generational and cherished Australian tradition.

Rides, jumping castles and sideshow alley provide memorable fun for the whole family when the show rolls into town. It's joyful to see kids light up as they make the most of the variety of activities on display.

But the show, as we know it, is on the brink of being a thing of the past. In fact, even the school or church fete, children's play centres, amusement parks and splash zones at caravan parks are all facing a clear and present danger.

The insurance crisis impacting Australia's amusement, leisure and recreation sector is threatening these family attractions, putting small and family businesses and thousands of jobs at risk. To put this into perspective, the sector employs over 7,000 people and contributes $1.84 billion to the economy in total.

A hardening global insurance market has meant that many small and family businesses in the amusement, leisure and recreation sector cannot get the essential insurance coverage they need to operate their business.

With only one insurer willing to provide coverage to these businesses, insurance premiums have skyrocketed – often by more than 200% - and many businesses have been refused coverage outright. Others have stranded assets, with just some of their equipment securing insurance coverage.

These business face imminent closure if they cannot get insurance. There will be significant job losses (particularly in regional areas), and a significant loss of economic activity in regional and metropolitan areas, will follow.

Our final report, The Show Must Go On, finds that a Discretionary Mutual Fund (DMF) is currently the only workable and durable solution for the industry.

Critically, this solution is reliant on foundational support from all levels of government, including legislative reform by all states and territories to ensure the DMF is accepted in lieu of insurance for licensing requirements. Additionally, the DMF needs to be recognised as a suitable solution at a local level and supported by councils, committees of management, showground managers and property owners hosting amusement, leisure and recreation activities.

Public liability insurance coverage is legally required across a range of businesses including rides at showgrounds, kids play centres, laser tag and even walking tours in national parks. This can be through contractual obligations as well as requirements imposed by State and Territory Governments on councils and other landowners.

As both our interim and final report details, DMFs operate to provide cover on a discretionary basis to a group of individuals or organisations which share a similar risk profile. Under the proposed DMF, members who meet membership requirements would have access to a certificate of protection, enabling them to operate their business, subject to the necessary legislative and regulatory change.

While this final report confirms a DMF as the most suitable solution, we acknowledge it is not a silver bullet. Among the challenges of the model, a DMF will:

- require an ongoing sector-wide commitment to best practice risk mitigation measures
- need to ensure membership remains cohesive and acts in the best interests of other members
- be unlikely to reduce coverage costs and these costs will likely increase in the short term
- not offer guaranteed protection for small business members, given the discretionary nature of the fund. While it is considered unlikely and not in the interest of the DMF to use its discretion to deny a claim, it

remains a possibility that could leave the small business owner open to liability

- may not satisfy all consumers. Consumers will need to accept some risk is involved with using amusement rides and participating in other leisure activities. This includes understanding they may not be covered in the event of injury if the DMF were to use their discretion to deny a claim
- likely attract high excesses compared to those previously paid, according to actuarial modelling.

Operating a DMF is not easy. It requires exceptional governance practices, including ensuring an appropriate balance of member representation with independent directors and specialist expertise.

Despite the challenges of the proposal, my office recommends the Australian Amusement, Leisure and Recreation Association's proposal to establish a DMF is the only suitable solution to the critical and immediate need for risk protection in the sector. Without a DMF, there is a real possibility the show cannot go on.

The findings in this final report should be read in conjunction with our interim report. These reports have been the subject of extensive and thorough consultation with stakeholders, including those in the insurance industry, the amusement sector and the mutual sector. I thank all of them for their time and expertise.

During our consultation with stakeholders and government, concerns were raised about possible heightened expectations in other industries interested in establishing their own Discretionary Mutual Fund. Policy parameters outlined in this report, including the requirement of significant market dysfunction, a clear and vulnerable membership base and the inability to self-fund, would, we believe, provide appropriate guardrails to deal with these issues if they arise.

We recommend the Australian Government provides appropriate 'seed capital' funding as a loan of up to $5 million (depending on actuarial advice and subject to 'best practice' DMF formation and operational conditions) towards the establishment of the DMF and works with State and Territory Governments to implement the necessary legislative changes as a matter of urgency. My office encourages the sector to finalise its plan for a best practice DMF as quickly as possible.

As the insurance crisis threatens the livelihoods of thousands of hard-working Australian small business owners along with many of the family entertainment activities that we hold dear, a DMF is the only suitable pathway forward.

Above all – the show must go on.

Hon. Bruce Billson

Australian Small Business and Family Enterprise Ombudsman

1. EXECUTIVE SUMMARY

1.1. Overview

1.1.1. Small businesses are consistently reporting insurance availability and affordability as one of the key barriers to their ongoing viability. This has been the case leading up to and since release of the then Ombudsman's inquiry into the affordability and availability of insurance for small businesses in September 2020.

1.1.2. The Ombudsman continues to work with various industry sectors, including the insurance sector, to investigate other options to ensure insurance coverage is accessible for all small businesses.

1.1.3. On 4 June 2021 the Ombudsman announced a self-initiated review of the Australian Amusement, Leisure, and Recreation Association's (AALARA) proposal to establish a Discretionary Mutual Fund (DMF) as a potential solution to the critical and immediate need for insurance in the sector represented by AALARA.

1.1.4. The review aimed to allow this Office to:

- provide further public policy advice following the interim report on the need to support businesses in securing critical risk protection products and compensation for consumers and
- investigate whether the DMF model proposed by AALARA would resolve the insurance crisis in the absence of suitable insurance products.

1.1.5. An interim report was released on 20 October 2021. Submissions were requested from interested parties by 3 November 2021. Twenty-five submissions were received from a range of interested parties including the amusement, leisure and recreation sector, showgrounds, regulators, the mutual sector, and the insurance sector. Some submissions included input from multiple businesses or organisations.

1.1.6. The interim report made preliminary findings that:

- A DMF suited the industry represented by AALARA
- A DMF may be a suitable way to address the insurance crisis faced by the industry
- The suitability and durability of a DMF solution for the sector would depend heavily on:
  - support for legislative reform from states and territories, including willingness to accept the solution by councils and land/showground managers
  - the final makeup of the membership
  - the cost of premiums and reinsurance, the management of the DMF and any management costs
  - the size of any claims in the first few years of operation.

1.1.7. The interim report proposed policy parameters for government considering support for a DMF, noting the possibility further sectors may request support to form their own DMFs to address insurance challenges for their sector. In particular, it seems likely that industries that are required by government to hold certain insurances for licensing requirements will seek government support in the event of significant market dysfunction.

1.1.8. The policy parameters recommended were:

- Significant market dysfunction or market failure must be established prior to government intervention

- The sector affected is unable to support establishment of a DMF in their own right
- There are no suitable alternatives for the sector to pursue, and therefore, the inability to secure insurance will lead to the loss of the sector or closure of a significant number of businesses within the sector
- There are other groups or entities outside of the sector likely to be negatively affected if the government does not take action.

1.1.9. Broadly, feedback received has agreed that while there is one insurance solution currently being offered to the sector (the Coversure-branded facility of the UK-based Aviva product), the sector believes that a DMF represents a more durable solution for their current difficulties in securing an affordable, durable solution to their insurance crisis.

1.1.10. Following the release of the interim report, the Ombudsman received advice from Coversure that it had secured the capacity to offer $20 million coverage as opposed to the $10 million originally being offered.

1.1.11. Concerns remain within the sector about the cost of the Coversure facility with multiple stakeholders reporting premiums of four to five times that previously paid in some cases. Concerns have also been raised about the capacity of the Coversure facility to cover the whole market, as well as the durability of their offering in Australia.

1.2. Findings

1.2.1. The interim review found that:

- A DMF suits the industry represented by AALARA
- A DMF is a suitable way to address the current insurance crisis facing the industry
- Support for legislative reform will need to be provided by states, territories, and local governments
- Local councils and land/showground managers will need to recognise and accept the solution
- Consumers should be made aware of possible limitations to the cover offered by the DMF.

1.3. Submissions received in response to the interim report

1.3.1. The Ombudsman thanks all who provided their views on the interim report, which have been invaluable to the preparation of this final report. Organisational contributors were:

- Adelaide Showground
- Allplay Equipment Australia
- Australian Amusement, Leisure, and Recreation Association Inc
- Coversure
- Edgewise Insurance Brokers
- Horseshoe Bay Water Sports
- Jetski Hire Magnetic Island
- Marsh Australia
- Melbourne Cable Park
- North Queensland Tours
- Play Australia
- Planet Entertainment
- Queensland Small Business Commissioner
- Redpath Cathcart
- Regis Mutual Management
- Royal Agricultural Society of NSW
- The Royal Agricultural & Horticultural Society of SA Inc.
- Sportscover Australia
- Sydney Royal Easter Show
- The Business Council of Co-operatives and Mutuals
- The Caravan Industry Association of Australia
- The Council of Small Business Organisations Australia
- The Insurance Council of Australia
- The Law Council of Australia
- The National Insurance Broker's Association
- The Newsagents Association of NSW and ACT
- The Showmen's Guild of South Australia
- Townsville Enterprise Limited
- Zoo and Aquarium Association

1.3.2. We also received submissions from individuals with an interest in the sector.

1.4. Terms of Reference

1.4.1. The Ombudsman's terms of reference initiated the review of the proposal by AALARA to establish a DMF for the amusement, leisure, and recreation industry. This work required significant engagement with industry through AALARA and related industry stakeholders. The review was to investigate whether the DMF model that AALARA and Aon proposed would resolve the insurance issues in the sector and may form the basis of further advocacy work by the Ombudsman in the insurance space.

1.4.2. As part of the Inquiry, the Ombudsman sought external advice, including specialist legal and actuarial advice. The Ombudsman also received advice from sectoral specialists in mutual insurance.

1.4.3. The Ombudsman's report considered the framework for formation of the DMF, the establishment phase (i.e. the first three years) and the DMF's ongoing operations.

1.4.4. In undertaking the review, and with the advice of external experts, the Ombudsman set out to:

1. Examine whether the cover provided by a DMF, and evidenced by a Certificate of Protection, will meet the requirements of members of the amusement, leisure and recreation sector to have public liability insurance as imposed by:
    a. Governments
    b. Licensing and regulatory authorities
    c. Contractual arrangements such as loan agreements, leases, and operating licences.
2. Consider any specific form of cover the DMF would need to provide or any specific contractual obligations that would need to be included in the DMF's policies in order to satisfy the above requirements.
3. Examine the minimum levels of cover and any requirements that members would be obliged to obtain from the DMF in order to meet legal obligations.
4. Consider whether a DMF comprising members of the amusement, leisure and recreation sector is likely to be financially viable on an ongoing basis, including identifying:
    a. The start-up and ongoing costs of the DMF
    b. Industry interest and likely levels of participation in the DMF, including whether larger industry participants will join (and impacts if they do not)
    c. What level of initial capital contribution to the premium pool will be required to ensure it is self-sustaining (i.e. can meet claims for a 1 in 200-year event, 1 in 100-year event, and 1 in 50-year event):
        - i. If the initial capital contribution is obtained via a loan, the expected time it will take the DMF to repay the loan
    d. The prior claims history of the industry, drawing on industry survey data and actuarial assessment
    e. How the DMF will operate in practice, including what level of claims will be funded through the DMF and what may be covered through reinsurance purchased by the DMF
    f. What form and amount of additional insurance the DMF will likely be required to meet claims not covered out of the premium pool
    g. Whether the required additional insurance is available in the current market
    h. What the premiums for the additional insurance are likely to be and whether premiums are affordable and commercially reasonable for DMF members (including how premium payments will be split between members)
    i. How DMF funds should be managed to ensure ongoing viability (of the DMF).

5. Outline appropriate legal and governance structures for the DMF, including considering measures the industry may be able to take in order to reduce the risk associated with the industry, and therefore insurance costs. This may include eligibility criteria for DMF members and ongoing eligibility verification.

2. REVIEW CONTEXT

2.1. Background

2.1.1. The amusement, leisure, and recreation industry has experienced extreme difficulty in accessing affordable public liability insurance for some time. This difficulty was highlighted in the AALARA submission to the then Ombudsman's 2020 Insurance Inquiry.

"We've been hearing from an increasing number of Members recently about a growing trend of insurance companies denying public liability insurance completely or pricing public liability insurance policies out of reach."[1]

In the time since AALARA's submission, the organisation has been working with insurance brokers, the Insurance Council of Australia (ICA), governments, various Ministers of the Australian Government, and State Officials to develop a solution to their members' inability to access public liability insurance.

2.1.2. Despite these efforts, AALARA received a letter from the ICA on 30 April 2021 which confirmed a likely ongoing inability of its members to access public liability insurance coverage. This points to an intractable failure within the Australian public liability insurance market for AALARA's membership, and the industry more broadly.

2.1.3. In response to the inability of their members to access affordable public liability insurance, AALARA has developed a proposal to establish a DMF for their sector. As part of its proposal, AALARA has approached the Australian Government to seek a capital contribution (as either a loan or grant), to assist with establishing an adequate claims capital pool and support obtaining reinsurance.

2.2. Role of ASBFEO

2.2.1. The Australian Small Business and Family Enterprise Ombudsman (ASBFEO) is an independent advocate for small business owners. Established in 2016 under the Australian Small Business and Family Enterprise Ombudsman Act 2015, the office assists and advocates for small business and family enterprises. The Ombudsman has legislative powers to conduct inquiries and research, work with other arms of government, contribute to inquiries and promote good business practice.

2.2.2. The Ombudsman's advocacy is centered on a number of issues small business raise with the office, including the availability and affordability of insurance for the sector.

1 Ahrens K, AALARA. *Submission to ASBFEO Insurance Inquiry,* August 2020

2.3. Terms and abbreviations

AALARA	Australian Amusement, Leisure and Recreation Association Inc.
AFSL	Australian Financial Services Licence
APRA	Australian Prudential Regulatory Authority
ARPC	Australian Reinsurance Pool Corporation
ASBFEO	Australian Small Business and Family Enterprise Ombudsman
ASIC	Australian Securities and Investment Commission
DMF	Discretionary Mutual Fund
DOFI	Direct Offshore Foreign Insurers
ICA	Insurance Council of Australia
NIIS	National Injury Insurance Scheme
MCIs	Mutual Capital Instruments
MNDF	Mutual non-discretionary Fund

3. THE PROBLEM TO BE SOLVED

3.1. Preliminary findings

3.1.1. The interim report found the hardening insurance market cycle is negatively impacting on the capacity of many businesses within the amusement, leisure, and recreation sector amongst others, to source appropriate levels of suitably affordable insurance. This 'hardening' or 'hard' market, driven by profitability and losses of insurance companies, was confirmed by the Insurance Council of Australia (ICA) in its report, Role of the Private Insurance Market – Independent Strategic Review: Commercial Insurance (the ICA Report).[2]

3.1.2. The issue of market failure or significant dysfunction was canvassed, noting that for many small businesses it is not possible to separate affordability of insurance from availability, as there is a price at which the insurance may as well not be available for purchase. While the ICA Report indicates that a 30-50% increase in premiums is in the 'medium' category of affordability, many small businesses report this is not the case. In fact, they are seeing increases in the order of 200%, and in some cases even more.

3.1.3. The impacts of this hardening phase of the market cycle and resulting market dysfunction, is that many businesses across a range of sectors, and particularly in the amusement, leisure, and recreation sector, are reporting an inability to source insurance. These impacts are being reported beyond the part of the sector offering show rides, and extending into related areas of active recreation, entertainment and activity centres, and even the experience-based visitor/leisure economy.

3.1.4. As highlighted in the interim report, without the statutorily and contractually required insurance coverage, the businesses in this sector will be unable to operate. This will lead to regional, rural, and metro shows, school fetes, carnivals and other events, being unable to offer rides and sideshow alleys, significant job losses, and stranded assets. Alternatively, there is a possibility that operators will continue to operate without adequate insurance, leaving consumers, showground operators, and business and landowners/property managers exposed in the event of an accident or injury.

3.1.5. The show rides and amusements are a key attraction of Australia's 580+ agricultural shows. Approximately 5.9 million Australians visit agricultural shows annually, contributing to an approximate direct annual economic value of $965 million[3], and total $1.84 billion once the tourism multiplier is applied.[4]

3.1.6. The interim report noted the critical importance of recognising that consumers have the right to peace of mind that their health and safety is protected, and in the event of an accident or injury, they will have access to adequate compensation. It is equally important that state and local governments, as well as showground operators, are assured of consumer protection through adequate insurance, as well as the landowners and managers themselves.

3.1.7. The case for a considered public policy response remains compelling and pressing.

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2 J Trowbridge, *Role of the Private Insurance Market – Independent Strategic Review: Commercial Insurance*, September 2021

3 QLD Chamber of Agricultural Societies Inc. *An Economic & Social Impact Study of Australian Agricultural Shows*, 2012 Page 1

4 Department of Resources, Energy and Tourism, Tourism Australia, *Tourism 2020, Whole of government working with industry to achieve Australia's Tourism Potential*, December 2011, Page 1

3.2. Feedback from stakeholders

3.2.1. Several stakeholders from the amusement, leisure, and recreation sector wrote of their considerable distress in being unable to find insurance in the current market. Several businesses highlighted the desperate need for a solution to this market dysfunction for there to be a hope of business survival. Businesses wrote about their long operating history, lack of previous claims, and concern about impending closure.

3.2.2. Sector representatives highlighted that where insurance is available, businesses are experiencing significant cost increases. One business stated the day prior to ceasing to operate in 2020, they were able to secure insurance from an overseas provider, at a premium increase of seven times the previous year.

3.2.3. Other stakeholders provided information about the increased cost of policies, with a $20 million policy coverage now costing $34,000 compared to $3,750 in 2019 and $7,950 in 2020.

3.2.4. Insurance sector stakeholders contend that insurance is obtainable, with the insured's risk profile playing a significant role in whether the business can be offered terms. These entities suggest the focus should be on risk mitigation rather than provision of additional insurance offerings.

3.2.5. One submitter stated that 'the reality within global insurance is that insurance is always available, at a price'. This contention is key to the question of significant market dysfunction for the sector affected by significant price increases as many businesses are unable to afford the price at which insurance is available, rendering it out of reach.

3.2.6. Several stakeholders highlighted a perception that government should regulate the operation and advertising of 'no win no fee' legal representatives, suggesting the actions of these parties that is driving up the cost of insurance.

3.2.7. We did not receive any submissions suggesting the sector was not facing a significantly dysfunctional market, and all stakeholders in agreement of a real and pressing need to address this dysfunction in some way.

3.3. Final recommendations

3.3.1. Having considered the range of high-quality submissions from stakeholders, we find the establishment of a DMF (as proposed in the interim report), remains the most appropriate way to address the amusement, leisure, and recreation sector's immediate insurance issues.

3.3.2. We recommend the Australian Government provide funding of up to $5 million guided by actuarial advice as to a necessary contribution to establishing an adequate initial capital pool. As outlined in the interim report, a grant might have been appropriate (perhaps on a $1:$1 matching basis) where the likely DMF members also contribute a significant proportion of the initial capital pool. This is not the intention under the industry proposal as the existing capital of the proposed DMF members is limited.

3.3.3. Provision of this funding should be conditional on:

- establishment of appropriate risk mitigation frameworks for DMF members
- appointment of a government appointee to the DMF board, to provide policy clarity and advice
- agreement that provision of services to the DMF will be contestable and contracted through periodic open and competitive tender process.

3.3.4. The timeline should proceed as advised in the interim report, aiming to establish the DMF within three to six months.

3.3.5. The hybrid model DMF proposed in the interim report and discussed below at 4.1.3 – 4.1.7, remains the most appropriate option for addressing the sector's immediate insurance issues.

3.3.6. In considering the volatility of the reinsurance market, the DMF should establish a plan to develop reserves like those required for APRA-regulated insurers.

4. OPTIONS FOR ACTION

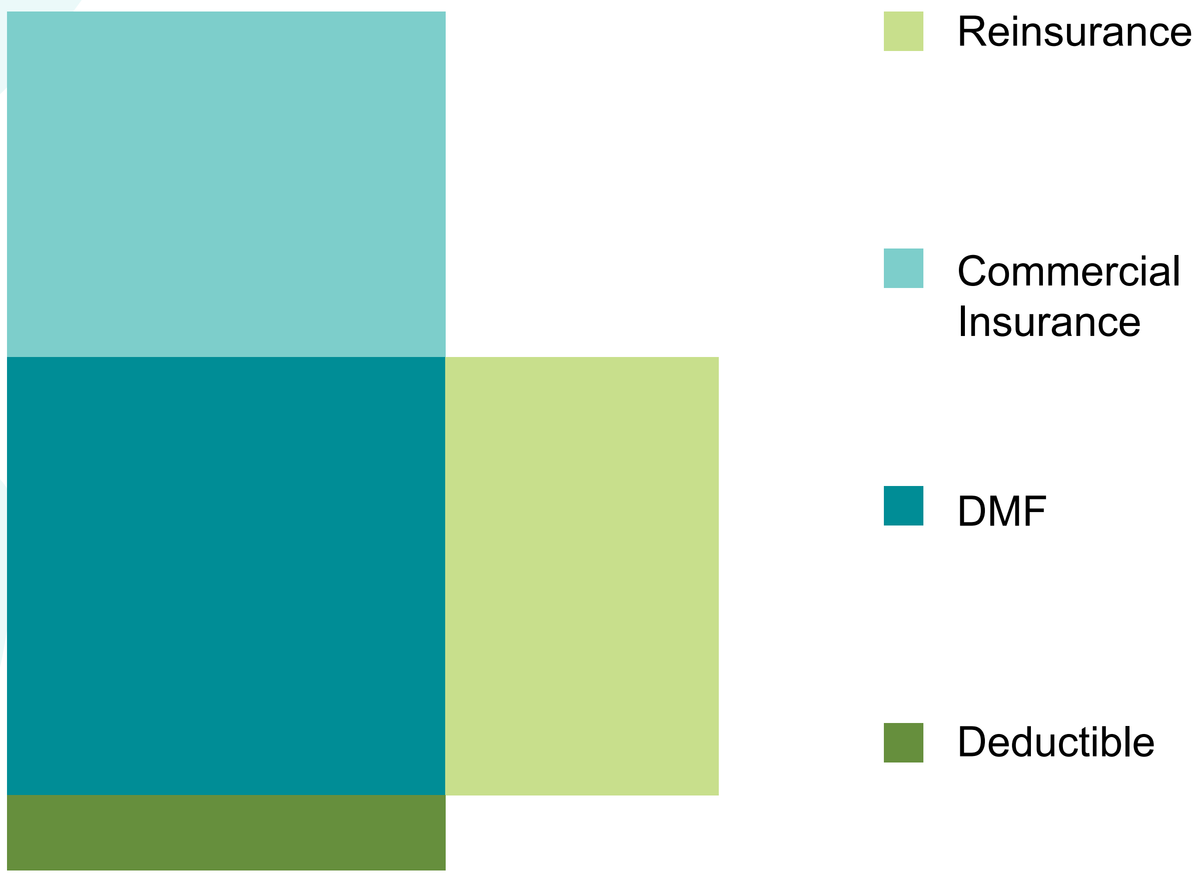
4.1. Preliminary findings on options for action

4.1.1. The interim report considered a DMF as the best path forward for the leisure and amusement sector, and canvassed several other potential solutions, providing reasons for their unsuitability. While some of these options would be considered stand-alone options, others may complement the proposed DMF in the longer-term as well as assist businesses in other industries in accessing certain insurance product classes. The options canvassed were:

- group insurance schemes
- establishment of a 'captive'
- self-insurance by the industry
- an Australian Government-backed reinsurance pool
- Tort law reform to establish statutory caps on compensation claim amounts
- the establishment, by the Australian Government, of a no-fault National Injury Insurance Scheme (NIIS).

4.1.2. A hybrid model for the recommended DMF appeared most suitable. Hybrid model DMFs collect premiums from their members and purchase insurance to cover and manage risk over and above the limit manageable by the mutual fund itself (the deductible). A new mutual will commonly cover 90% of its risk by reinsurance and decrease this percentage as the fund's reserves grow.

4.1.3. The hybrid model proposed in the interim report is based on that adopted by the Activities Industry Mutual in the United Kingdom.



4.1.4. Under this structure, the DMF is triggered once a threshold deductible retained by the member is exceeded. The interim report noted the appropriate level of deductible will need to be considered and determined proportionately to a member's capacity to pay, and risk exposure. This is important as it encourages good risk management and good claims practices, by ensuring a 'pain threshold' before DMF funds become available.

4.1.5. The proposal included in the interim report, is that the DMF would cover any cost above the deductible, supported by 'reinsurance' or 'excess claims insurance' to protect the DMF against loss. This excess claims insurance needs to be drafted to allow for the fact that the DMF extends indemnity on a discretionary basis, and the insurer will need comfort around the exercise of that discretion.

4.1.6. The interim report noted the need for excess claims insurance will be greater in the early years while the DMF is building capital, noting that reinsurance may not always be available to the level required, or at an acceptable cost.

4.1.7. As proposed in the interim report, the DMF could then purchase an 'excess layer' of commercial insurance above the DMF, allowing the DMF to act as a 'deductible in-fill'. This addition would provide a right to indemnity, removing the risk of discretion for members and, critically, third parties reliant on the cover available to the member. The insurance layer could kick in at lower levels when insurance is available and commercially attractive to reduce the retained risk in the DMF. While commercial insurance may not always be available, the DMF rules should be drafted in such a way that commercial insurance can be added as another layer of protection on the DMF when it is available.

4.1.8. As previously mentioned, risk protection provided by a DMF is discretionary in nature and a DMF is unable provide its members a certificate of currency as a traditional insurer would. Certificates of currency are often critical for accessing lending and licensing as well as council approvals for land use. A hybrid model may provide a solution to the certificate of currency issue as the group reinsurance policy would provide greater certainty to those accepting business membership of a DMF in lieu of insurance, where insurance is not available in the market.

4.2. Feedback from stakeholders on options for action

4.2.1. Several submissions provided feedback on questions relevant to the options for action canvassed by the ASBFEO, as well as providing comments on those options in the Interim Report.

4.2.2. Feedback from some stakeholders felt there was insufficient detail on why a group insurance policy has been ruled out and suggested that a group insurance solution may be possible. While it may be the case that further actuarial advice may allow the revisiting of group insurance, we understand the sector has already explored group insurance and been advised it is not available to them.

4.2.3. Some submissions suggest that where a DMF is being considered to avoid future volatility in the insurance market, the hybrid model suggested would not achieve this. Stakeholders suggested that 'the reinsurance market is far more volatile than the insurance market'.[5] Stakeholders shared the view that the proposed DMF will be heavily reliant on reinsurance for the first few years after formation.

4.2.4. Multiple organisations supported tort reform along the 'New Zealand model' in their submissions.[6] Some suggested that a business in New Zealand would pay a fraction of the cost for a 'like for like' insurance product.

5 Sportscover Australia Submission in response to 'The Show Must Go On' Report, 27 October 2021.

6 Support was received in submissions from Melbourne Cable Park, Planet Entertainment, the Townsville Enterprise Limited, the Queensland Small Business Commissioner, the National Insurance Brokers Association, and the Caravan Industry Association of Australia.

4.2.5. Organisations suggested the lack of statutory caps for injuries has led to a proliferation of 'no win no fee' litigation. These organisations suggested that the operation of 'no win no fee' litigation ultimately increases insurance costs through encouragement of spurious claims that insurers often pay as they make the assessment that payouts cost less than defending claims in court.

4.2.6. One organisation spoke of their insurer paying out a claim despite finding the injury being the result of 'intentional misadventure by the customer'. The assertion was that paying the claim was deemed cheaper than defending the claim.

4.2.7. Stakeholders pointed to the period of time when New South Wales banned advertisement of 'no win no fee' legal services, and pointed to a reduction in claims during that period.

4.2.8. It was broadly agreed that the legislative change required across multiple jurisdictions will not be an easy or quick process but that the long-term reform to tort law would be beneficial for the sector. It was suggested by some that sustainability of a DMF would depend on reforms from state and territories.

4.2.9. The establishment of a 'no blame compensation injury fund' was proposed by stakeholders, as well as legislative reform to 'lower the cost of risk transfer'.

4.2.10. Some stakeholders indicated in-principal support for the DMF as a temporary solution to the challenges facing the sector while 'sustainable, long-term solutions for affordable insurance (such as tort reform and a NIIS) are explored.

4.2.11. Sectors that sit outside AALARA's membership, but are facing similar issues in obtaining public liability insurance, strongly supported the proposal for a government-backed, hybrid model DMF. These stakeholders have signalled an intention to seek DMF membership for their members.

4.2.12. Stakeholders from the mutual sector highlighted their confidence in an industry owned and operated DMF to lift risk management standards and improve safety outcomes for the sector.

4.2.13. Some provided further recommendations including:

- promoting risk management and better standards
- transparency with the membership (through member control of the board)
- sub-committees including a claims committee so that Member Directors have oversight of the core protection issues affecting members and the DMF.

4.2.14. The proposal for a hybrid model, whereby the DMF seeks insurance above a manageable deductible, was welcomed by stakeholders. The benefit of a hybrid model was thought to encourage the DMF to follow claims in a very similar way to insurance claims.

4.2.15. Other stakeholders provided qualified support for the proposed DMF while providing insights built on experience managing discretionary trust schemes. Specifically, it was suggested the proposed DMF may wish to voluntarily employ similar compliance and best practice rules as regulated insurance companies.

4.2.16. The analysis of perceptions of the discretionary nature of DMFs included in the interim report were endorsed by stakeholders. Sound analytical and actuarial models were identified as vital to facilitate the involvement of the insurance sector. Known and identified points where insurers can collaborate with the DMF will support the participation of those insurers.

4.2.17. One submission suggested that instead of a DMF, it would be preferable to establish a mutual non-discretionary fund (MNDF). The submitter proposed a MNDF would operate in a similar manner to the proposed DMF, however, the MNDF would have a legal obligation to pay claims. As such, while this proposal would increase the predictability of claims payment, it is effectively a general insurer, which would require prudential regulation (akin to that of a general insurance company) by the Australian Prudential Regulatory Authority (APRA).

4.2.18. The recommendation of a MNDF reflected concerns that the discretionary nature of the proposed DMF posed too high a risk to small business members whose claims the DMF may refuse. Despite the associated costs, the submitter was troubled by APRA not regulating the proposed solution. This concern is addressed by the DMF adopting best practice governance and operating standards.

4.2.19. It is important to note APRA regulation would require the fund to retain significantly higher capital, rendering the current proposal inoperable. We note there are existing Australian DMFs who have retained capital up over several years to align with APRA standards without undertaking to become APRA regulated.

4.2.20. There is no reason the proposed DMF could not have this as a goal.

4.2.21. As noted in the interim report, we understand DMFs rarely use their discretion to deny claims outright but do use it to challenge spurious claims and those of dubious merit. The use of discretion to deny claims outright would be detrimental to the DMF as members would need to seek alternative protection. DMFs can therefore use the discretion available to them to defend claims a traditional insurer would simply pay out to protect immediate profits.

4.2.22. Some stakeholders, particularly those from the insurance sector, suggested the sector may need to take on a greater portion of risk than currently, and/or pay a higher financial impost for the transfer of risk onto the insurance market. This additional risk or financial impost would need to be addressed through increased premiums and a greater number of excluded activities. This is unlikely to be viable for an industry where many businesses are currently barely able to meet insurance premium payments.

4.2.23. For businesses that have faced significant challenges as a result of public health orders over the course of the COVID-19 pandemic, excluding some of their activity offerings, will impede recovery by lessening available revenue streams, and create medium to long-term stranded assets.

4.2.24. Insurance industry stakeholders suggested that sectoral risk could be further limited through operational actions including standardised 'active' risk management delivered by industry associations. One submission provided a list of gaps in risk management and mitigation policies and procedures the submitter believes exist in the sector. It is suggested that addressing these concerns, possibly using public funds that would otherwise be made available for the proposed DMF, would have an immediate impact on the risk transfer cost for the sector.

4.2.25. It should be an aim of the proposed DMF to use its pooled resources to lift the collective risk management and mitigation of its members. Stakeholders agreed that industry commitment to develop and implement good risk management should be a key requirement for government support of the proposed DMF.

4.2.26. Stakeholders also pointed to existing mutuals' practice of excluding potential members with poor risk management practices. This would contribute to the longevity of the DMF but could also restore insurer confidence in the market, aiding the DMF's pursuit of excess claims insurance.

4.3. Final observations and findings on options for action

4.3.1. Tort reform, reform of advertising 'no win no fee' legal services, and the establishment of an NIIS were strong themes throughout the submissions received. These may warrant further consideration, as they will benefit not just the proposed DMF and its members but address a broader range of insurance availability and affordability challenges facing a range of small and family businesses.

4.3.2. The recommendation that the proposed mutual seek to become prudentially regulated has been put forward in the interest of the mutual's members. While this will not be possible from the DMF's inception, building a capital pool that meets prudential requirements should be a long-term goal in line with better practice considerations.

5. DISCRETIONARY MUTUAL FUND DEFINED

5.1. Preliminary findings about Discretionary Mutual Funds

5.1.1. The interim report provided a history of mutual funds, and specifically DMFs from their inception in England in the late 17th Century. Mutual funds have been established across the globe, and are often established by specific occupation groups in the absence of suitable protection or savings solutions from the general insurance sector.[7]

5.1.2. A mutual entity typically comprises a group of individuals with common risk profiles or goals that pool financial resources to meet agreed financial risk obligations of each member. Members typically own and operate the mutual entity. Mutuals are known to operate most effectively where there is a regular pattern of relatively small losses as opposed to infrequent catastrophic losses.

5.1.3. As such, responsible and robust risk management is crucial to the long-term viability of the entity. The DMF can, and should, play a role in the implementation of membership-wide, tailored risk mitigation practices.

5.1.4. Generally, each member of the mutual has one vote, regardless of the level of premiums paid into the mutual,[8] except where the mutual decides to issue Mutual Capital Instruments (MCIs) as outlined under 2019 amendments to the Corporations Act 2001.[9]

5.1.5. The sector saw a wave of demutualisations across the developed world in the late 20th century, before DMFs became more popular again as industry sectors have sought solutions to hardening insurance markets, or wish to retain profits for the sector rather than paying them to a third party company's shareholders.

5.1.6. DMFs do not commonly provide public liability insurance, and those that do primarily exist in the UK and in some circumstances in local governments in Australia.

5.1.7. DMFs operate to provide risk cover on a discretionary basis to a group of individuals or organisations. While discretionary protection is similar to traditional insurance, there is a critical difference.

5.1.8. Under traditional insurance coverage, a policy holder has a contractual right to have their claim paid upon meeting the policy's terms and conditions. In contrast, a DMFs members, who are also its owners, are entitled to submit a claim for indemnity to the DMFs board (or management entity), who may or may not approve the claim, at its discretion.

5.1.9. This discretion to deny claims is rarely exercised, and is usually exercised in favour of the member where claims that may fall outside policy guidance or protection guidelines are paid to enable an early resolution and to avoid the need for claimants to pursue the member directly via formal legal action.[10]

5.1.10. DMF members therefore do not have the same legal claim to indemnity against an event that holders of traditional insurance products do.[11]

5.1.11. Approved claims are paid from a common fund made of pooled member contributions that are similar to premiums paid under traditional insurance coverage.

5.1.12. It is important to distinguish between DMFs, which are not regulated by APRA, and authorised mutuals, who provide contractual insurance cover and are subject to prudential regulation.

7 Swiss Re, *Sigma 4. Mutual insurance in the 21st century: back to the future*?, Swiss Re, 2016, p 2
8 G Potts, *Review of Discretionary Mutual Funds and Direct Offshore Foreign Insurers*, 2004, p 18
9 *Corporations Act 2001* (Cth), ss 167. AB-AJ.
10 G Potts, *Review of Discretionary Mutual Funds and Direct Offshore Foreign Insurers,* 2004, p 17
11 G Potts, *Review of Discretionary Mutual Funds and Direct Offshore Foreign Insurers,* 2004, p 17

5.1.13. DMFs are particularly effective in thin or hard markets, where the sector:

- seeks to address a lack of insurance availability or affordability
- is easily defined
- is cohesive
- has sufficient capital to establish the DMF and manage the first few years' of claims.

5.1.14. DMFs benefit from their deep knowledge of the sector, enabling them to exclude industry members with higher risk profiles and reduce the likelihood of claims. Typically, DMFs manage claims against their members very closely, often successfully defending claims other insurers may have paid.

5.1.15. DMFs can be at risk of management capture where the sector does not have sufficient appropriately qualified representatives to manage the mutual, with the support of a mutual manager for the first few years of operation if necessary. The interim report highlighted the importance of ensuring the mutual manager does not completely control the operations of the mutual, with concerns raised throughout consultations about mutual managers encouraging reliance on the management company rather than encouraging development towards self-sufficiency.

5.1.16. The interim report also pointed to the need to ensure a DMF is a durable solution for the sector, by guarding against possible future demutualisation. Demutualisation becomes attractive where member engagement with the mutual is low, or where the market failures the DMF was created to address are less severe and members consider that they may be better served by broader market providers. Members may benefit financially from the division of resources that have been built up over the years or possibly generations.

5.1.17. The durability of a DMF will be threatened unless the leadership can demonstrate benefits of membership over and above, in this instance, addressing the absence of accessible and affordable insurance coverage.

5.1.18. DMFs are popular internationally, covering a range of risks including medical indemnity, motor vehicle, home and contents, property, and professional indemnity.[12] However, cover for public liability is not common under a DMF structure.

5.1.19. Best practice and elements for a DMF to succeed generally include:

- ensuring an appropriate structure: advisers to this project prefer the Company structure due to the greater suitability for providing good governance over a longer period, and the ability to raise MCIs
- operating with full funding, or having sufficient funds to meet the highest realistic amount of claims cost that is retained before external reinsurance is triggered
- sound governance processes that involve an appropriate balance of member, management and independent expertise
- appropriate reinsurance or excess claims insurance, which is arguably the most important element of security for a DMF, particularly in the early years.

5.1.20. It is important for the government to determine whether there is an appetite for regulating DMFs through APRA, such as was suggested by the HIH Royal Commission, or to consider that DMFs continue not to pose a systemic risk and that regulation by APRA is unnecessary, as suggested by Mr Potts in the Potts review. This aspect is addressed in feedback and consultations.

12 International Cooperative and Mutual Insurance Federation (ICMIF), *Members*, ICMIF website, n.d.

5.1.21. There be key criteria for any consideration of potential government support of a DMF, which could include:

- **Evidence of market failure or significant dysfunction.** This does not mean only that there is a hard market but should also include consideration of whether there is commercially available insurance that provides sufficient coverage for the industry at an affordable price. Further, governments may consider reducing legislatively required amounts of coverage required to help make insurance more affordable and available.
- **Consideration of potential membership base,** including whether it would be appropriate to allow business to be denied support from the DMF on the basis that they are not a member of a proponent industry association. Further, there should be consideration of the broader economic and social benefit the businesses provide.

5.1.22. The interim report noted that DMFs are a proven model for delivery of insurance type products where members show considered commitment and meet requirements. However, it also noted that regulatory and legislative barriers to various parties accepting membership of a DMF in lieu of insurance need to be addressed.

5.1.23. The interim report discussed the key requirement for legislative and regulatory change across States and Territories, including at local government level, to consider DMF membership as sufficient in lieu of insurance for the purpose of legislative and contractual requirements.

5.1.24. Consideration of whether a DMF would be acceptable for service users, noting that consumers may not fully appreciate or consider the risk, is important.

5.1.25. The interim report also considered whether site owners and managers would be willing to accept a DMF, or a lower coverage than the current statutorily required $20 million.

5.1.26. DMFs are subject to significantly less regulation than traditional insurance, however they do operate with a degree of regulation, with the requirement of an Australian Financial Services Licence (AFSL) to be held by the manager. This means DMFs can provide financial protection to their members, but the protection is not generally recognised in legislation. Due to the nature of a DMF, in normal circumstances there is not a practical significance to the lack of regulation, as claims are made in a very similar way to insurance claims.

5.1.27. APRA does not regulate DMFs. The idea was canvassed in the Potts Review, although Mr Potts noted that it seemed inconceivable that DMFs could pose any sort of systemic risk given their small market share.[13]

5.1.28. Following a subsequent discussion paper by the Treasury, the Australian Parliament passed the Financial Sector Legislation Amendment (Discretionary Mutual Funds and Direct Offshore Foreign Insurers) Bill 2007 (DMF and DOFI Bill) on 13 September 2007. This allowed APRA to collect information on DMFs, however APRA revoked its relevant reporting standards and ceased collecting data on the industry in 2016.

5.1.29. Despite not being subject to APRA regulation, some DMFs employ APRA prudential benchmarks in managing their capital holding.

5.1.30. The Australian Securities and Investment Commission (ASIC) regulates the national corporate, financial services, consumer credit and authorised financial markets. To conduct financial services business, an Australian Financial Services Licence (AFSL) is required, which would be needed to legally manage a DMF.

13 G Potts, *Review of Discretionary Mutual Funds and Direct Offshore Foreign Insurers*, 2004

5.1.31. An AFS Licensee has several obligations, relating to:

- conduct and disclosure
- training and competence
- compliance
- managing conflicts of interest
- risk management (among others).

5.1.32. Further, ASIC has significant information-gathering and investigative powers. Where the employment of these monitoring tools reveals license breaches or other contraventions of the relevant acts, ASIC has the legislative power to take a range of enforcement action.

5.1.33. The interim report noted that a defined DMF membership base with shared interests is important. This consideration should be balanced with the capacity of a larger membership base to increase revenue streams that allow for expanding reserves and provide for healthy cash flow.

5.1.34. Establishing a DMF requires significant setup costs. This is particularly true as initially the DMF will be vulnerable to large claims in the event of a catastrophic event. Securing insurance, or having the ability to rely on members to provide capital, may be required and members must be aware of these potential risks.

5.1.35. One strategy to prevent large claims against the DMF is to include strict conditions of membership and risk mitigation. This is a key benefit of a DMF, as members will often mitigate risk more effectively, giving the DMF greater claims defence capacity.

5.1.36. As discussed in Section 4, the interim report provided a proposal for a DMF structure, known as a hybrid structure, similar to that adopted by the Activities Industry Mutual in the United Kingdom.

5.1.37. The interim report highlighted the importance of risk mitigation and standards, as the foundation of the DMF. Some suggestions to help ensure risk management is achieved and accepted include, effectively training board members, standardising risk mitigation measures, adoption of existing risk and regulatory schemes, and creating positive relationships with insurers and reinsurers.

5.1.38. The interim report noted that the DMF should aim to become self-sufficient as soon as possible. To achieve this, a strong culture of risk mitigation, rigour around membership, commitment to the longevity of the DMF, and diligence around funds administration, will need to be embedded within the organisation, through a committed and capable board. The report noted that the majority of the board will be required to be members of the fund and should have industry experience along with a strong interest in the success of the DMF. Further valuable skills will include legal, financial, or corporate management skills.

5.1.39. If it is determined that taxpayer support is conditional on a government representative, this person should bring a strong overview of the ongoing public interest supported by the DMF, and commensurate accountability to the board.

5.1.40. It will take between three and six months to set up the DMF, however six months is a more realistic timeline given the complexities of establishment.

5.2. Feedback from stakeholders on Discretionary Mutual Funds

5.2.1. Many small businesses, their representative associations, and showground operators passionately supported the proposed DMF solution, noting that a scheme of this kind would enable their businesses and industries to survive. A range of industry bodies submitted, noting that membership of the DMF should not be restricted to those businesses that are members of a particular industry body.

5.2.2. Some sector small business stakeholders and their representatives submitted that a DMF could be an appropriate short-term solution, while concerns remained about rising claims numbers which will need to be addressed in the longer-term.

5.2.3. Further exploration of sustainable, long-term solutions for affordable insurance in this sector and other small business sectors was also encouraged by stakeholders.

5.2.4. Insurance sector stakeholders noted that a DMF may be a viable solution, although the performance of differenct DMFs will vary. These stakeholders noted that for the DMF to be a durable solution, it must be comprised of a very committed group of long-term members, committed reinsurers, and have depoliticised policy and business management so that it can operate without interference.

5.2.5. Some insurance sector participants noted a preference to have the opportunity to comment on a final, not conceptual proposal, including accurate claims history and risk profiles of industry members.

5.2.6. Mutual sector representatives broadly agreed that formal commentary is challenging without a completed proposal to assess.

5.2.7. A range of stakeholders submitted that without tort law reform, the DMF will struggle to stay afloat.

5.2.8. Many stakeholders agreed with the statements in the interim report that a critical precursor to DMF formation is that all levels of government legislate to accept DMF membership in lieu of insurance. Many also noted that others such as clients of the businesses will also need to accept the DMF membership in lieu of insurance.

5.2.9. Stakeholders that currently manage DMFs noted that APRA regulation for discretionary vehicles may cause many existing DMFs to cease operation. They suggest that were APRA to regulate DMFs, community organisations currently utilising DMF structures would be disadvantaged and pushed out of solutions that are currently working well in a non-APRA regulated environment.

5.2.10. Conversely, stakeholders from the legal industry strongly favour APRA regulation of any eventual solution, noting that greater regulation of DMFs was recommended by the HIH Royal Commission.

5.2.11. Complexities around AFSL licensing were raised, suggesting that compliance creates a barrier to creating a DMF. Obtaining an AFSL is beyond the means of most small businesses and as a result, the majority, if not all, DMFs established in the past 10 years have been established under the umbrella of another appropriately qualified licensee through an intermediary authorisation.

5.2.12. The solution proposed by AALARA is not to require individual DMFs to hold an AFSL, but that licensees who act under intermediary authorisations to issue DMF products should be required to notify this activity to ASIC.

5.2.13. A Mutual Management organisation recommended that government consider amending legislation to allow brokers to deal in mutual products, provided it is for general advice only. They also proposed amendments that grant DMFs an automatic exemption if they wish to limit membership to certain groups or associations.

5.2.14. Precedents of legislative acceptance of DMFs was noted by stakeholders, in particular the example of the South Australian State Government updating legislation to recognise the Public Liability “insurance” arrangement used by South Australian local government councils.[14]

5.2.15. It has also been noted that any solution will need to evolve over time, for example if the legislative requirement for insurance was increased from $20 million to $25 million. Another example from South Australia was provided, where the local sector’s minimum level of cover has been increased. Any solution will need to remain vigilant around potential changes to ensure relevance and ‘stickability’ of members.

5.2.16. Several stakeholders noted that the suitability and long-term sustainability of a DMF will be dependent on necessary legislative reforms from state and territories.

5.2.17. Appropriate risk management frameworks were highlighted as critical by many stakeholders, although some noted enforcement of high standards (in order to exclude industry members with higher risk profiles), may result in many amusement and leisure operators not being accepted into membership. Some of these stakeholders believe focusing on risk mitigation is a more sustainable path than establishing a DMF.

5.2.18. Some common concerns regarding risk that could be addressed to improve affordability include:

- low-cost parks operating without adequate supervision such as unattended swimming pools and insufficiently staffed water slides
- minimal or no CCTV to log allegations of, or actual, claims and injuries
- use of equipment not verified to comply with Australian Standards/state regulators
- under-developed risk analysis, procedures, and training, including some cases where operations manuals do not match the activity
- inadequate or unconsidered adverse weather alerts, warnings, safety or protection
- inaction in response to past claims
- waivers that are not updated to changes in Australian Consumer Law.

5.2.19. Various stakeholders suggested that risk management could be enacted through limiting membership of the DMF, and such an approach should be avoided to allow for a larger membership base. Overwhelmingly it was agreed that significant investment in risk management initiatives should occur from launch. A quick and effective option to encourage good risk mitigation procedures was suggested to be to educate members through high-level information about losses. Such an approach should not aim to name and shame members who have had claims made against them, but highlight what happened, why it happened and how it could have been prevented.

5.2.20. Holistic responses from industry to mitigate risk are seen as important. Such an approach could include freely available template documents, case studies, and accreditation and verification. The emphasis here is on self-help tools that are widely and easily accessible.

5.2.21. Generally, support was provided for the proposed structure as a company limited by guarantee.

5.2.22. Regarding board membership, stakeholders suggest:

- frequent rotation of board members, with a maximum term of 10 years
- service contracts subject to frequent open market, competitive tender, with a maximum appointment of 5 years
- any promoter receiving remuneration, either directly or indirectly, should be disclosed to members in renewal documents, annual reports and annual financial statements.

14 *Local Government Act 1999* (SA), s 142.

5.2.23. Stakeholders noted that despite the timeline being achievable to set up the DMF, the timeline to place insurance may require extra time. Further, stakeholders recognised the changes required for all levels of government to accept the DMF as an alternative to insurance may take some time.

5.2.24. Some stakeholders suggested that governments will need to accept a level of risk if they provide support for the proposed DMF.

5.2.25. Some stakeholders suggested there is the opportunity to expand the remit of the Terrorism Insurance Pool through the Australian Reinsurance Pool Corporation (ARPC).

5.2.26. Some insurance sector stakeholders suggest that as insurance is still available at an admittedly high price, the sector is not experiencing market failure, and it is likely a DMF will face the same pricing issues.

5.2.27. It is important to note that significant market dysfunction was also pointed to in the interim report, as an acceptable marker for government support for a DMF.

5.2.28. Several stakeholders spoke about concerns around ‘no win no fee’ lawyers increasing the likelihood of spurious claims being made, many of which are paid out as insurers see the cost of a payout as likely to be less than the cost of defending a claim.

5.2.29. Some stakeholders noted the benefits of a DMF adopting (and eventually normalising) industry standards above minimum requirements. For example, the minimum statutory period for delivery of a renewal notice for insurance contracts is 14 days, however, a DMF could operate on a longer timeline and provide 30 days’ notice.

5.3. Final observations and findings on Discretionary Mutual Funds

5.3.1. Subject to the conditions outlined in 3.3.3, the most appropriate and immediate solution for the current insurance crisis facing the amusement, leisure and recreation sector is the proposed DMF.

5.3.2. Governments at all levels should begin immediate work on amending legislation to allow for DMF membership to be accepted in lieu of insurance for the purpose of public liability. This could be based on South Australian legislation allowing operation of a local government mutual.

5.3.3. It may be prudent for the Treasury to play an enabling role in supporting the states and territories in this work and to coordinate working groups and information sharing among the jurisdictions as appropriate.

5.3.4. Legislation should also be amended to allow brokers to deal with mutual products, provided it is for general advice only.

5.3.5. The design, risk management and governance suggestions proposed in the interim report should be adopted.

5.3.6. Consideration by policy makers of ways to mitigate increasing premium rises should continue. These could include:

- a review of the ‘no win no fee’ litigation industry
- further government support and regulation.

6. GOVERNMENT SUPPORT

6.1. Preliminary findings in relation to government support

6.1.1. The interim report noted the importance of ensuring that government intervention in a market such as this should only, and always, be a last resort in the event of an inability to source a product or service on the open market at affordable prices. The interim report then provided examples of previous government intervention, including in the medical defence sector after the collapse of HIH insurance, in establishing the Terrorism Reinsurance Pool, and most recently in establishing the Northern Australia Cyclone Reinsurance Pool.

6.1.2. Where government intervention in a market is contemplated, clear conditions for support need to be developed including a possible government appointee on the board for the life of any financial support, a financial structure that allows for the repayment of the loan if applicable, and guarantee of competitive, regularly contested, and independent contracts for the fund management, legal and actuarial services provided to the DMF.

6.1.3. A determination of market failure or significant dysfunction by an independent and authoritative source is a critical precursor to any government intervention in the insurance market. The interim report suggested that once this determination is made, a group of specialists in DMF development could be deployed to provide advice to the business sector on the set up of a DMF.

6.1.4. Suggested additional supports for newly formed, or forming, DMFs proposed included template documents and pathfinders that could be provided in an open-source format, and the possible establishment of an expert taskforce within Treasury to provide best practice assessment and analysis of future DMF proposals. Encouragement was also given to engagement with the existing mutual sector and broader ecosystem, through close engagement with established DMFs, the industry body, the Business Council of Co-operatives and Mutuals.

6.1.5. Options for government support included funding made available for addressing risk issues in the sector, seeking specialist advice, setting up the mutual, and funding to support an adequate capital pool.

6.1.6. The interim report considered whether a loan to be paid back, or a matched grant would be most appropriate, given the strong feedback from stakeholders particularly in the mutual sector of the importance of the membership base having ‘skin in the game’ by taking ultimate responsibility for some, if not all, of the start-up costs.

6.1.7. The proposed board make up was that of nine members, with five being members of the mutual, one being a government appointee, and three independent experts with expertise in insurance (ideally mutual insurance), law, risk management, and/or actuarial modelling.

6.1.8. It was also suggested that consideration of apportioning board representation from the membership base might be appropriate to avoid the possibility of voting blocs developing which may lessen the democratic nature of the organisation.

6.1.9. The interim report further recommended consideration be given to how to optimise market participation. It was suggested that this could be achieved through seeking commercial insurance from the market, where possible and appropriate, as well as through ensuring they operate as a good corporate citizen in line with public and stakeholder expectations of the broader sector.

6.1.10. The acceptance of the DMF solution by states, territories, local councils and other interested stakeholders was highlighted in the interim report as a critical element of the success of the solution. Without this acceptance, the DMF will not provide adequate cover for potential members to continue operations.

6.1.11. Perceptions around the discretionary nature of the cover were raised, noting that this is a key challenge to the success of a DMF. The idea that the discretion leads to a lower requirement to pay claims was refuted by the sector, pointing to a view that the discretionary nature and board determination powers of a DMF enable the fund to operate in the grey areas of claims in a way that often allow claims to be paid out, even where there is no strict requirement to do so.

6.1.12. The issue of legislative change and perhaps harmonisation to allow membership of a DMF to satisfy legislative requirements to hold insurance where insurance is not available was canvassed.

6.1.13. Recognising the complexity of separate state and territory legislative amendments, it is acknowledged that in some instances Commonwealth legislation can 'override' State legislation. The relevant legislation would need to relate to a Commonwealth power under the constitution.

6.1.14. For certainty and predictability around the acceptance of a DMF, it is preferable for states and territories to implement the necessary legislative change where 'insurance' is required by statute. However, legislation could be considered by the Commonwealth, with the agreement of the states and territories to bring about legislative change and to ensure appropriate recognition and acceptance of this notion at a state and territory level. Whilst it is theoretically possible for the Commonwealth to initiate overriding legislation, this is likely to be highly contested and does not address the implementation factors at state, territory, and local government levels, needed to support the implementation of a DMF.

6.1.15. Safety and operations standards and verification were canvassed, pointing to a range of Australian and international standards that should be the base line of compliance for future DMF members.

6.1.16. Issues of consumer awareness of the nature of a DMF were also canvassed, highlighting the importance of disclosing the nature of the cover provided to consumers and allowing them to make informed choices about their risk appetite.

6.1.17. A proposal for partial 'self-insurance' by consumers through an offering such as Flip Insurance was also canvassed.

6.2. Feedback from stakeholders on government support

6.2.1. Many stakeholders supported the proposed grant funding model, suggesting the model would allow the industry to develop a long-term solution and look after itself.

6.2.2. Others suggested that a matched grant was just one option for the provision of start-up funding, noting the model may unintentionally penalise smaller groups or associations.

6.2.3. Alternatives proposed in submissions from stakeholders to a matched grant as proposed in the interim report were:

- a capped grant which could be related to size, possibly with a minimum contribution percentage by members, noting that this model creates a situation where a proportion of the membership is asked to subsidise the start-up costs of others who join later
- a government draw-down facility, repayable when the DMF has a sufficient level of surplus from its ordinary activities. Repayments could be undertaken by instalments which are a fixed, or scaled, percentage of surplus
- financing options to fund insurance premiums for the industry, noting that this would not address issues of expensive premiums or large deductibles payable at a time of loss
- full indemnification for industry participants. It was noted, this would not necessarily address risk concerns across the sector and could create a dangerous precedent for other industries who may find themselves in comparable situations
- bank guarantees or loans, the costs of which could be budgeted for when calculating member contributions
- identifying other mechanisms to build the DMF's capital base and long-term financial sustainability, including possibly applying capital levies to be paid by members, along with accumulated surplus
- crowd funding start-up capital.

6.2.4. Noting these ideas, the DMF as proposed in the interim report will allow short-term Government support while providing a mechanism for industry, not the Government, to carry and address risk. Further, the proposal creates a blueprint for future potential government support of other industries in a manner that meets public expectations on risk mitigation and public spending.

6.2.5. There was broad support of the governance and reporting standards outlined in the interim report, with a range of stakeholders recognising them as appropriate for a DMF. One stakeholder suggested that a government appointee acting as a representative on the board may result in conflict. They suggested this conflict could be resolved if the Government appointee were to hold a standing invitation to board meetings as an observer instead of sitting on the board.

6.2.6. One stakeholder suggested that it is too early in the proposal development to set the required number of directors and composition given the size of the potential DMF is not yet known.

6.2.7. Stakeholders from the mutual sector supported the need for independent directors with skill sets required by the board, while highlighting the importance of enshrining member democracy.

6.2.8. One stakeholder suggested it may be more prudent to initially have a majority of specifically skilled, independent directors on the board with a minority of member representation. This proposal is not appropriate as mutual entities are required to have a majority of member-directors. As such, this Office does not support recommendations to move control of the proposed DMF from the membership to independent directors. The independent directors should instead support the member-director leadership.

6.2.9. Several stakeholders provided views on the interaction of a DMF with the legal jurisdictions of Australia's states and territories. One suggested that in the absence of a mechanism by which the DMF could provide an insurance certificate, such as a group insurance policy that sits above the DMF retention, a government guarantee could be a potential solution.

6.2.10. This Office does not support a government guarantee as an acceptable level of risk for the Australian Government to carry. Such a proposal may also be viewed as a precedent for other sectors and DMFs, potentially exposing the government to carrying further risk on behalf of industry that should otherwise be seeking market-based solutions.

6.2.11. Several stakeholders highlighted and supported the interim report's commentary on issues around the perception of discretion, with some suggesting that the largest concern is from third parties who require evidence of insurance. Again, the proposal for a government guarantee was raised to address issues with discretion, and this proposal is not supported by this Office.

6.2.12. The banking sector has indicated that acceptance of DMFs may vary significantly across banks based on their individual risk appetite. As such, potential members of a DMF should work closely with their banks to ensure acceptance of the solution if necessary.

6.2.13. As previously discussed, several insurance sector stakeholders urged consideration of increased enforcement of safety and operating standards across the industry to create a more conducive path to insurance certainty than may currently be the case.

6.2.14. Specific suggestions for improvement include:

- utilising digital records that follow the National Audit Tool for Amusement Devices to increase visibility and lift standards
- developing an insurance industry-supported educational program to support increased risk mitigation measures within businesses.

6.2.15. In line with all comments provided on the safety environment in which the sector operates, the proposed DMF should mandate safety and operating standards to ensure all members meet, and indeed exceed legal requirements. This will help protect the capital reserves and integrity of the DMF.

6.2.16. On the matter of consumer awareness of use of a DMF in lieu of insurance, some stakeholders suggested that there is little difference between the DMF proposed and the use of an insurance policy maintained by a business. Additionally, stakeholders suggested that a DMF may create opportunities for members where a risk framework could be promoted to consumers as part of their service or facility use.

6.2.17. It was broadly agreed that the current disclosure of risks through clear printed information on notices or tickets should be maintained.

6.3. Final observations and findings on government support

6.3.1. The comments provided by stakeholders did not alter the Ombudsman's position that the proposed loan model of government support is the most efficient solution for the sector while remaining in line with community expectation use of public funds.

6.3.2. Further consultation on the board make-up may be appropriate during the final design phases.

6.3.3. The DMF should work to centralise legislative considerations and provide current resources to its members.

6.3.4. Notwithstanding the conceptual scope for the Commonwealth to introduce overriding legislation, uncertainty and possible inability to properly support the recognition and acceptance of a DMF as a suitable substitute for insurance means that timely legislative action at a state and territory level is essential for the success of the proposal. State and territory action will also assist in ensuring commensurate recognition and acceptance of the DMF at a local government and landholder level.

6.3.5. Considering the importance of an adequate capital pool at the commencement of a DMF, and in the absence of member capacity to provide for such a pool, there is a compelling case for government assistance of up to $5 million by way of a loan. Actuarial advice will determine the appropriate level of support.

7. INDUSTRY LEADERSHIP

7.1. Preliminary findings on industry leadership

7.1.1. The interim report noted the importance of ensuring the DMF membership is clearly defined and suggested that it could be leveraged via industry association memberships, while ensuring that such membership is not a precursor to entry.

7.1.2. Several sectors could be covered by the proposed DMF, including AALARA’s membership, the Showmen’s Guild membership, the caravan park industry, and the adventure tourism industry.

7.1.3. One of the key justifications for the sector seeking government support to establish the DMF, is the substantial social and economic contributions the leisure and amusement industry makes, and an inability to fund an adequate capital pool that supports early claims and access to excess claims coverage.

7.1.4. The local show is a hub for regional communities to come together and participate in a range of commercial activities and social events, which promote a strong sense of community, purpose and celebration of participation and success. Other important benefits include providing children and younger people the opportunity to develop leadership skills, identity and education.

7.1.5. Beyond the local shows, the sector provides much needed domestic recreation, venues for active events for children, support for local school and church fetes, and fundraising opportunities for community organisations. The sector also provides significant tourism value, and opportunities for both domestic and international tourists to learn more about Australia’s natural environment.

7.1.6. The proposed DMF is critical in supporting businesses, industries, regional economies and communities to prosper into the future.

7.1.7. The interim report acknowledges that there are several factors acting concurrently that have led to the current substantial insurance premium increases or unavailability of insurance cover. There is a lack of participating insurers operating in the leisure and amusement sector, and a perception of higher levels of future claims risk for the sector.

7.1.8. Following release of the interim report, AALARA and Aon completed their actuarial modelling for the proposed DMF. This modelling was independently verified by Finity, and advice on the viability of the proposed model provided to this Office.

7.1.9. As the interim report highlighted, for the DMF to operate as an ongoing and compliant structure that can meet its liabilities (claims and costs) and continue as an on-going concern, strict risk management and governance protocols need to be adhered to, to protect members and consumers. The interim report proposed DMF entry requirements as follows:

- agreement to abide by, and be audited against industry-developed safety standards that are no less rigorous than the Australian and international Standards, and updated regularly as best practice develops
- provision of a complete record of past claims that accurately reflects a 'good' claims history against industry norms
- agreement to undertake training as required by the DMF Board
- agreement to submit to 'spot audits' of equipment should the board require it
- commitment to bring all potential claims to the DMF within a specified time frame, including providing an undertaking not to attempt to 'self-manage' claims
- acceptance of an excess and accompanying low level claims management protocols
- consideration may be required as to refusing coverage for certain operators, machines and/or activities deemed by the board to be higher than acceptable or manageable risk or unable to be adequately mitigated.

7.1.10.This list of possible DMF entry requirements is not intended to be comprehensive or complete and should be adjusted according to needs identified during the DMF's development.

7.2. Feedback from stakeholders on industry leadership

7.2.1. A number of stakeholders from outside the AALARA membership expressed an interest in either joining this DMF or establishing their own. One manufacturer of playground equipment submitted that '…we were close to shutting our doors last year when we unable to secure Professional Indemnity'.

7.2.2. A policy for $5 million coverage was subsequently obtained, however the cost increased from $3,700 to $26,600 per annum. The policy cover has now been increased to $10 million which has incurred further cost increases.

7.2.3. While the requirement to hold Product and Public Liability coverage of $20 million for each claim has not increased, the cost has doubled.

7.2.4. Engineers and others whose role is to maintain rides and other amusement equipment, are also seeing increases in their insurance cover and are likely to be negatively affected in the event of an accident. For this reason, some stakeholders suggested the DMF cover should be extended to Professional Indemnity insurance.

7.2.5. A number of stakeholders pointed to the need for industry leadership, particularly where previously separate business groups may be coming together to form the DMF. Stakeholders from the mutual management sector urged caution about 'forcing a marriage' between differing business groups to naturally fit into the same DMF.

7.2.6. These stakeholders pointed to the fact that successful DMF's have membership bases made up of entities who are comfortable to share risks with each other, have a commonality of activities, and an understanding of those activities which can be used to develop better standards and improved risk management. The commonality of risk is essential to ensure no sector of the membership ends up cross-subsidising another.

7.2.7. Stakeholders suggested that the entry requirements proposed in the interim report were adequate, and will be dependent on the DMF's definition of a member as set out in the constitution. Thereafter, the board will have the power to determine further entry requirements, and retain absolute discretion over the acceptance of members.

7.2.8. Some concern was raised that if the entry requirements are set too strictly, many businesses currently struggling to secure insurance will be excluded from the proposed solution. Should this occur, it is hoped that the sector as a whole would support industry participants to raise their standards to improve consumer safety, reduce claims numbers, and ultimately provide better risk profiles to both the DMF and other insurers.

7.2.9. A range of stakeholders agreed that the 'success features' identified in the interim report were accurate and appropriate. Some suggested additional opportunities, including ensuring that members commit to a minimum membership period to provide stability of funding.

7.2.10. The possibility of AFCA membership for the DMF was also canvassed, with a suggestion that such membership would provide further certainty and comfort to industry participants, as well as consumers.

7.3. Final observations and findings on industry leadership

7.3.1. In the short-term it is critical that AALARA finalises the development of its DMF proposal, and that the necessary research, development and implementation is expedited.

7.3.2. There are no additional broad industry sectors that should be included in the initial membership of the proposed DMF, although consideration could be provided in the future to expanding the membership pool.

7.3.3. Given the identified complexities of establishing a DMF, combined with the time constraints, it would seem appropriate for the DMF membership to be initially focused on AALARA and Showmen's Guild members and near-associated industries.

7.3.4. Initially focusing membership on AALARA and Showmen's Guild members should assist the DMF to:

- set risk priced contributions for small businesses
- seek long-term members from aligned businesses
- develop policies, procedures and protocols for members to mitigate risks)
- develop, adjust and evolve to insurance market and legislative changes.

7.3.5. It may be appropriate for aligned, but not closely related, industries to consider establishment of industry-specific DMFs, should they be experiencing ongoing and significant market dysfunction.

7.3.6. The DMF management should apply best practice principles, to provide the leadership, mentoring, guidance and culture for the DMF to develop, evolve and grow in line with stakeholder's expectations and predetermined benchmarks.

7.3.7. Once the DMF is established it may take on long-term commitments via 'long tail' claims. An actuarial review of the claims history of the sector suggests that there could be a delay between a causal episode and the lodgement of a claim. As such, prospective DMF members should look to make longer-term commitments to the DMF, to ensure the fund has the required capital to meet its obligations.

7.3.8. As previously discussed, there is a critical need for all levels of government to explore the opportunities and willingness for legislative change to assist with managing the quantum of public liability insurance claims, whilst meeting the public's expectations for consumer protection.

7.3.9. Consideration should be given to ensuring the DMF is able to become a member of AFCA.

7.3.10. Should a market softening eventuate then the DMF will need to have additional offerings that will allow it to compete for new members and retain existing members in a lower cost market. Consideration should be given to this eventuality in the DMF's business planning.

8. IS A DMF FIT FOR PURPOSE?

8.1. Preliminary findings on fitness for purpose

8.1.1. The interim report highlights the need for clear definition of the DMF's membership. It also highlights a need to remove the perceptions of cross subsidisation of the membership.

8.1.2. Ashurst however noted the importance of having a diverse membership pool to diversify risk.

8.1.3. To counteract the possibility of discontent between the members, Ashurst has recommended the implementation of risk management and audit programs, premium incentives for members with low claims histories, co-insurance for bad risks, and putting an aggregate limit on a members' right to coverage in one year.

8.1.4. The interim report also highlights profit incentives for members who may seek to demutualise and capitalise on intergenerational build-up of resources. The interim report suggested that the DMF should be designed to guard against demutualisation.

8.1.5. The interim report further proposed that to bolster industry support and membership commitment, the board should engage regularly with their members to drive cultural cohesiveness. Members need to be involved as much as possible in shaping the direction, risk mitigation processes, and culture of the DMF. Such activity will help differentiate the DMF from general insurers and promote non-financial benefits of the scheme including 'value add' training and technical services.

8.1.6. This office has previously recommended development of a process to ensure safety requirements and operator standards are reliable. This could be achieved through developing standard procedures, requirements for safety and maintenance to be documented, and making these activities a condition of membership in the DMF. In addition to these documented standards, an accreditation process is considered beneficial.

8.1.7. 'Stickability' was determined to be unlikely to be an issue where there is a lack of insurance, however as the insurance market softens, the DMF may struggle to retain members. As the DMF is not designed to return profit to shareholders, the DMF will likely have little in the way of capital reserves to push premiums lower if the market softens.

8.1.8. It was recommended that alternative offerings to increase stickability should be developed over time, including:

- industry training
- recognition amongst consumers (e.g. tick of approval)
- business support
- group buying to discount commonly used items and services
- marketplace or brokerage services.

8.1.9. The interim report identified the mutual manager must be trusted to support the sector, have specific knowledge of the directors and drive the best outcome for the DMF.

8.1.10. The perceived conflict of interests of brokers acting as the mutual manager were noted, with suggestion that consideration should be given to addressing and ensuring ongoing management of any perceptions of conflict of interest of the mutual manager.

8.1.11. A periodic, open and competitive process to reappoint fund managers and service providers was recommended. It was further recommended the length of the initial contract should be short and renewed at one-to-two-year periods or at a five-year review.

8.1.12. The interim report suggested that once any initial loan from government is repaid, or if determined at the five year review, the DMF may consider the appropriateness of entering longer-term contracts with service providers. The initial short-term contracts will allow the government to have confidence in delivering value for the public through their capital investment.

8.1.13. Careful management of claims handling by the mutual manager and the board, was highlighted as critical to DMF success.

8.1.14. Concerns about the discretionary nature of a DMF leading to valid claims being denied were canvassed in the interim report, however the international and domestic mutuals point to a culture where claims are rarely denied. The intention of the boards of these entities is 'to do the right thing' by their members and consumers.

8.1.15. Such an approach needs to be supported by:

- sufficient financial reserves
- clear internal policy parameters
- a clear statement of exercised discretion not setting a precedent for future claims.

8.1.16. A newly established DMF needs to be able to deny and defend claims it considers to be spurious to avoid a reputation amongst the legal profession as a 'soft touch'.

8.1.17. Some mutuals that commence operation as discretionary mutuals convert to become 'authorised mutuals', offering formal insurance products. This can be achieved by retaining members and increasing the capital reserves of the organisation.

8.1.18. The interim report noted that the DMF must enjoy public confidence, at least among members and customers of members, to be successful. It is also worth considering whether the DMF should, through its members, undertake targeted consumer education campaigns.

8.1.19. For consumers, disclosure around risks will be key and it was proposed that the DMF should consider providing members with documents that explain the nature of the DMF, why it has been developed, and provide information about the claims process in the event of an incident necessitating a claim. The DMF could also provide the necessary support to answer consumer queries.

8.1.20. Following a few years' operation, the DMF may also provide businesses with information that consumers may find useful, for example the number of claims received and the typical result of these claims.

8.1.21. The interim report recognised that a successful DMF needs to interact with the broader market through its operations and recognising the market dynamic will allow for securing excess claims cover and commercial insurance (perhaps as a buying group) for claims above a certain amount.

8.1.22. Best practices examples, both internationally and domestically, maintain strong relationships with international insurance providers, including reinsurers, so that the DMF can place insurance and reinsurance with the best value providers.

8.1.23. It may also be beneficial for the DMF to engage with the mutual sector in Australia and overseas to gain understanding of which international insurers have the greatest knowledge of, and provide the most support for, the Australian mutual sector.

8.1.24. The interim report highlighted that prior to the establishment of the proposed DMF, work will need to be undertaken with state and territory governments to address the threshold issues of legislative recognition/acceptance and preferably harmonisation required to accept membership of a DMF in lieu of insurance.

8.1.25. Again, the interim report highlighted that without the co-operation of state and territory legislatures, the Australian Government alone cannot ensure success of a DMF.

8.1.26. The interim report suggested that should the Australian Government decide to support the DMF proposed by AALARA, and following a review of the final proposal developed by Aon in partnership with AALARA, government will need to undertake the following actions:

- finalise the type of support to be provided, whether it is a grant, a low interest loan, or another form of support including 'gap' insurance and/or reinsurance enablement
- determine and appoint a government representative for the DMF board
- enter into the necessary agreements with AALARA and/or the board of the DMF
- assemble and make available a nominated policy-lead and technical and regulatory expertise to expedite DMF formation and the development of guidance material.

8.2. Feedback from stakeholders in relation to fitness for purpose

8.2.1. A number of stakeholders raised a future softening of the insurance market as presenting a significant challenge to the proposed DMF's 'stickability'. These stakeholders supported provision of additional services to strengthen the DMF's value proposition. They also supported regular engagement between the mutual managers and members to strengthen relationships and to build member commitment.

8.2.2. Consideration of the potential GST and other tax implications that may arise if additional services are provided will be necessary.

8.2.3. The importance of the DMF utilising better practice guides, reflecting on individual experiences, and providing examples of when to make a claim as a way to create a strong relationship between insurers and the insured, was highlighted by a number of stakeholders.

8.2.4. In particular, where a claim is submitted for consideration, or a potential member is denied entry, the DMF should proactively engage with those industry participants to uplift risk management, mitigation, and practice to support DMF membership, reduce risk related contributions, and avoid potential future claims.

8.2.5. One submitter suggested use of a digital safety management system to be deployed among all DMF members. This would standardise the way that risks are identified and communicated and support member retention.

8.2.6. Another solution offered by stakeholders is that of a 'capital levy' which involves members making upfront payments to build capital reserves for the fund. These funds would be available for return to members of the fund upon demutualisation.

8.2.7. As addressed elsewhere in this report, the existing capital of the proposed DMF's members is limited, meaning they are unlikely to be able to meet a capital levy at the proposed DMF's inception. However, such a levy may be able to be raised later as economic conditions around the sector improve and could be enabled by the judicious use of mutual capital instruments.

8.2.8. Stakeholders have noted the importance of contestability of service contracts to the DMF, to reduce real and perceived conflicts of interest.

8.2.9. Concerns were raised about short-term management contracts being insufficient in length to ensure that managers can set up the fund and invest in its longevity. It was suggested that sufficient time needs to be provided for building relationships with stakeholders, such as the board and reinsurers. Five years was the recommended time frame for a management contract to allow for the consistency of management.

8.2.10. Stakeholders welcomed the need for a review after a number of years and it was noted that such a review could be a condition for government support.

8.2.11. While some fund proponents expressed support for Aon to manage the fund given their work on its development, others recognised that due to the expected initial capital support from government, public expectations would be that there is an open and competitive process to select a mutual manager and other service providers.

8.2.12. Insurance sector stakeholders highlighted the importance of good risk management by members, and the impact this would have on accessibility of insurance for the fund.

8.2.13. Some from the insurance sector suggested that the role of the DMF is to create a risk environment where competition is created between insurers. It was suggested that this could be achieved on a portfolio basis (i.e. a panel of insurers underwriting all risks on a proportionate basis), or a per-risk basis (i.e. individual risks within the DMF are brokered to select insurers).

8.2.14. Insurance sector stakeholders noted that best practice claims handling processes combine efficient handling with controls that anticipate losses and reduce frequency. Consistency in claims handling, through both disciplined processes and a steady team of claims managers, create an environment where trends can be identified, and controls and policy structures adjusted accordingly before losses accumulate. Empowerment of relevant claims staff working for the mutual is essential in achieving this, with delegation of adequate authority to take decisive early action to reduce claims costs.

8.2.15. Overall, stakeholders highlighted that it is important that claims handling is efficient, and discretion is exercised fairly. It is seen as important that the DMF embraces a culture of risk mitigation and management and ensures that policies are adaptable to address trends and potential risks.

8.2.16. Stakeholders did not see an immediate need for government legislation to prevent demutualisation, however, it was agreed that controls of some form are needed to ensure effective use of funds should the fund demutualise.

8.2.17. Some submissions highlighted the possibility of a structure that allows members (not the board) to vote in favour of a major changes to the structure of the organisation, including on demutualisation, and that such motions would only be affirmed once a high proportion of members have voted in favour (e.g. more than 75% of members, i.e. a 'super majority').

8.2.18. Stakeholders recognised that while having mechanisms that allow for demutualisation would enable the members to decide the fate of the DMF, where government support has been provided for the establishment of the fund, it is important to ensure that demutualisation does not result in member enrichment.

8.2.19. There were conflicting views on the public's likely confidence in the proposed DMF.

8.2.20. Some stakeholders raised concerns about consumers not understanding the DMF without proper education, resulting in consumers not having sufficient information to make informed decisions about participation in certain activities.

8.2.21. Other stakeholders noted that mutuals appear to be well established throughout Australia, and as such does not believe that public confidence is likely to be an issue, and that securing insurance for the fund would lend further public confidence.

8.2.22. Overall, stakeholders have expressed the importance for the DMF to engage with insurers, reinsurers, brokers and other mutuals to ensure that the DMF is able to keep up to date with claims handling procedures, understand key industry issues, and identify opportunities to access insurance or reinsurance. This close engagement will also assist the DMF with risk management and risk mitigation.

8.3. Final observations and findings relating to fitness for purpose

8.3.1. Provision of services above and beyond public liability insurance to ensure member value should be carefully considered by the DMF in its development phase.

8.3.2. In considering these additional services, the DMF proponents will need to seek appropriate tax advice about GST implications for the fund.

8.3.3. To ensure value for money and public confidence, it is important to have an open and competitive process to appoint a mutual manager and other service providers. Given stakeholder feedback highlighting that short-term contracts may not allow for effective management, consideration should be given to longer contracts of 2 to 3 years to ensure the DMF management is effective.

8.3.4. Claims handling processes should be established to allow for quick, effective, and fair claims handling. Any discretion must be enacted equitably to ensure member loyalty.

8.3.5. It is also important for the DMF to embrace a culture of risk mitigation and disciplined claims processing.

8.3.6. Government should further consider regulating demutualisation, and consideration needs to be given to a mechanism that prevents member enrichment through demutualisation, especially whilst a loan is being repaid to government.

8.3.7. The DMF should create materials to educate or provide support to consumers, so they are aware of how a DMF operates so that they are able to make informed decisions about risks prior to engaging in activities.

9. NEXT STEPS

9.3.1. This report will be delivered to the responsible Ministers and the Department of the Treasury for their consideration.

9.3.2. Consideration will need to be provided by the Government as to whether to support the formation of the DMF, and what conditions they may place on such support.

9.3.3. Based on the available information, there is a need for Government to consider what is assessed to be a credible case for government to provide capital in the form of a loan, subject to the best practice governance and implementation we have provided in the interim and final report, including the inclusion of a government appointee to highlight public policy requirements.

9.3.4. Early engagement with state, territory, and local governments to address the legislative reform issue will be critical to the success of the DMF.

9.3.5. The DMF proponents should consider what additional steps they can take to expedite the formation of the DMF, including but not limited to:

- development of the DMF constitution and other formation documents
- seeking taxation advice, particularly regarding implications of additional service delivery to members
- further consideration of the actuarial modelling to ensure final membership fees and forecasting is as robust as possible.

APPENDIX A – INTERIM REPORT CONSULTATION QUESTIONS

The consultation questions proposed in the interim report are included below. We did not ask each respondent to respond to all consultation questions, but that some would provide broad input in relation to their area(s) of expertise.

1. Is there a need for action by government? Is there a proven incapacity for the industry to self-support a solution?
2. If the government does not act to support the sector, what alternatives could the sector pursue?
3. Are there any other groups or entities likely to be affected if the government does not take action?
4. Are there any other options for action that should be considered by the sector or the government?
5. What other aspects of DMF better practice should be considered?
6. Are the public policy considerations listed accurate? Should additional considerations be included?
7. Is there sufficient evidence that a DMF, if appropriately formed and governed, could work for the various stakeholder groups?
8. Are there other regulatory considerations that should be addressed?
9. Are the design, risk management, and governance suggestions appropriate?
10. Does the timeline appear reasonable?
11. Are there alternative examples of government intervention that should be considered?
12. Are there other aspects that should be considered in terms of market conditions or capacity building for the DMF board and membership?
13. What alternative models of financial support could be offered?
14. Are the governance and reporting proposals appropriate? Is the suggested board make-up likely to provide the best results for the DMF?
15. Are there other issues that need to be considered in relation to interaction with states and territories?
    a. Are the perceptions around discretion presented accurate? Are there other perceptions that should be considered?
    b. Are there specific legislative barriers that should be considered?
16. Are the current safety standards/regulatory environment/Quality Assurance verification purposes fit for purpose? If not, how would you suggest these be amended?
17. What needs to be undertaken to ensure consumer awareness around the DMF? Are there alternative methods for consumers to manage their own risk?
18. Are there other sectors that should be included in membership of this DMF?
19. Are the proposed DMF member entry requirements adequate? What additional requirements could be considered?
20. What else should be considered in the process of the final proposal development?
21. Are the key success features identified accurate? Are there other features that should be considered?
22. What other offerings to the DMF membership might increase ‘stickability’?
23. How important is contestability of service offerings? Are there other ways to ensure contestability?
24. What are additional best practice claims handling procedures?
25. Should the DMF include a constitutional protection against demutualisation? Should government introduce a protection against demutualisation for the broader sector?

26. Is public confidence in the DMF likely to be an issue? What else could be done to encourage public confidence in the proposed DMF?

27. Are there appropriate mechanisms to reengage with private sector/industry market solutions over the life of the insurance market cycle? If not, what proposal settings would enable the sector to take advantage of a softening market?