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LOGICAL FINANCIAL MANAGEMENT
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PRESSURE ON PREMIUMS AS DISASTER BILL PASSES \$5 BILLION

Insured losses from the spate of natural disasters which hit Queensland, Victoria and Western Australia last summer have reached \$5.4 billion, placing further pressure on premiums for commercial and domestic policies.

Topping the list are claims arising from flooding and heavy rains in south-east Queensland which are now estimated to be worth \$2.6 billion, according to the Insurance Council of Australia. Cyclone Yasi, which hit north Queensland, has reached \$967 million.

The flooding and severe storms which occurred in Victoria in January and February have totalled \$399 million and Perth's bushfires have accounted for \$35 million.

The unprecedented series of disasters has unsurprisingly sparked speculation about what impact they would have on premiums.

Surveys of insurers conducted in the second half of 2010 and reported midway through the summer suggested a "two-speed" market, with premium increases for domestic lines but a softer commercial insurance market driven by competitive pressures and excess capital. But the extent of the devastation became clearer by the end of the December-January period which has led to a reassessment of the impact on rates.

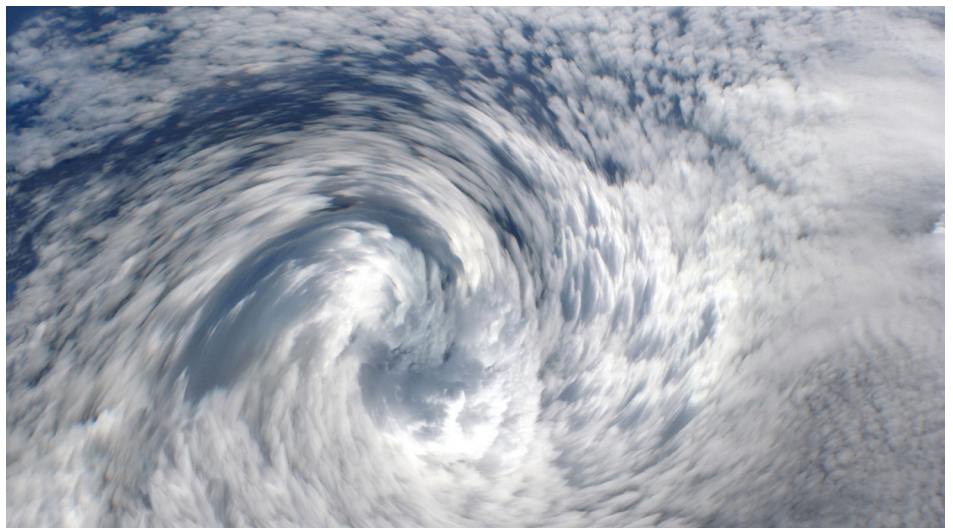
There have been predictions that reinsurers, hit hard by the disasters in Australia as well as the New Zealand earthquake and the earthquake and tsunami in Japan, could

increase rates by 20-30% or more in the Asia-Pacific region when some insurers renew their cover in June, in turn flowing on to premiums.

Recent devastating tornadoes in the US could further soak up excess global capital in the international reinsurance market, removing a buffer for extended price rises.

Anecdotal evidence from brokers suggests that insurers are looking very closely at individual clients' risk when deciding how to price it or whether to provide cover at all. Rates for commercial lines of insurance hit by recent disasters, such as buildings and equipment, are most affected.

Commenting on this environment, National Insurance Brokers Association CEO, Noel Pettersen, said: "In these circumstances it is even more important to get advice from your broker and to pay close attention to risk management in your company."



SCRUTINY OF INSURANCE HERALDS SWEEPING CHANGES TO FLOOD COVER

Unprecedented scrutiny of insurance since the catastrophic flooding which hit south-east Queensland and Victoria in December and January will determine how policyholders are protected in future disasters.

Following widespread confusion amongst owners of inundated properties about what they were covered for, and a range of definitions of flood being used by insurers, the Federal Government initiated reviews to develop a standard definition and to examine the availability of cover to individuals and businesses for damage and loss associated with flood and other natural disasters.

The Federal Treasury issued a discussion paper on a uniform definition of flood to be used by all insurers to either cover it or exclude it in their policies:

Flood means the covering of normally dry land by water that has escaped or been released from the normal confines of:

A. any lake, or any river, creek or other natural watercourse, whether or not altered or modified; or

B. any reservoir, canal, or dam.

BROKERS SUPPORT STANDARD DEFINITION

Brokers' views have been represented by the National Insurance Brokers Association (NIBA). In its submission NIBA agreed that a standard definition will go a long way towards ending policyholder confusion, but questioned whether an alternative form of words should be used.

"The difficulty with the term 'flood' is that a consumer's understanding of what the term may or may not mean...is very broad, as is the case with the typical dictionary definition," the submission said.

NIBA also suggests that policyholders could be advised on where to obtain information on the flood risk of their area, for example from the local council, and encouraged to seek advice about what cover they need from a licensed expert if they are unsure.

NIBA warned that the standard definition and other proposals would not address some issues that commonly arise in relation to flood claims, notably, what is the cause of the damage if there is a mixture of flood water and storm water, yet flood is excluded in the policy.

A solution could include making an independent expert's opinion as to the cause of damage binding on both parties and legislative changes clarifying what happens to claims when flood water and storm water combine.

"Appropriate advice from professionals such as insurance brokers can assist in reducing confusion and the proposed change will make it easier for insurance brokers to advise their clients," NIBA said in its submission.

DISASTER INSURANCE PAPER RELEASED

Meanwhile, the Natural Disaster Insurance Review, established by Assistant Treasurer and Minister for Financial Services and Superannuation, Bill Shorten, has just issued a discussion paper looking at a range of issues, including how to make flood cover more widely available to property owners.

The options in the paper are full flood cover, with all insurers compelled to offer cover for all insured properties, an opt out provision that allows property owners to insure without taking flood cover, and the status quo in which insurers are free to offer or not offer cover.

The paper notes that under the first option disputes over whether the damage was caused by storm or flood water would be eliminated, but property owners in flood prone areas would pay substantially higher premiums unless there was some form of subsidy or discount.

Funding for such a subsidy would need to come from governments (taxpayers), councils (ratepayers) or insurance (other policyholders), all of which required further examination.

ISSUES FOR SMALL BUSINESS

The paper also looked at the specific problems facing small businesses, the majority of which do not have flood cover. Small business owners, who are more likely to use a broker, have more specialised insurance requirements, are more price sensitive and less likely to purchase additional cover such as flood insurance.

The number of insurers providing small business insurance is limited, and any compulsion for them to provide insurance cover could see some withdraw from the market, reducing competition and pushing up costs.

NIBA CEO, Noel Pettersen, said anecdotal feedback from brokers with clients in flood affected areas showed the lessons learned were much the same as for householders -- be aware of the likely impact of flood on your business, heed warnings from the authorities and be prepared, if possible, to move stock and equipment.

"Brokers have said they would welcome flood cover being more widely available, but priced separately so the client could decide whether they wanted to pay the additional cost," he said.

INSURERS WANT BROADER DEBATE

Insurers have also expressed concern that a requirement to include flood cover in all policies would override individual underwriters' appetite for risk and would not discourage householders and businesses from building in flood-prone areas

They have called for a broader debate on how governments at all levels deal with mitigating flood risk, including mapping, planning, zoning and building standards.

The Federal Attorney General, Robert McClelland touched on these issues when he recently told a conference that perhaps the Federal Government should consider putting more funds into mitigation and resilience measures rather than just doling out relief payments after each disaster.

"Put simply it is counter-productive if government assistance acts as a disincentive to people taking steps to build their own resilience -- such as taking out insurance. I believe we need to be more strategic and more ambitious than just getting people back on their feet -- only to be knocked down again.

"We need to look at minimising our exposure to disaster risks over the short, medium and long term -- and this means focussing as much on prevention and mitigation as on recovery," he said.



WHAT POLICYHOLDERS AND BROKERS THINK

Recent surveys of brokers and policyholders have given an insight into how each views the impact of natural disasters.

A survey of brokers commissioned by insurer Vero, and conducted by Sweeney Research, found the majority (23%) saw natural disasters as the biggest challenge facing the commercial insurance industry. This was followed by negative perceptions of the industry (18%), under-insurance (16%) and insurance taxes and fees (15%).

“Insurers are pumping billions of dollars into the community and are a major provider of economic stimulus – \$12 million is being spent in Queensland every day by insurers. The challenge though is to ensure this contribution is understood by the community.

“To do this, we need to ensure our product and service standards are of excellent quality for our customers.

“That’s our number one responsibility as insurers and brokers and how we can make a real difference,” said Andrew Mair, Executive General Manager of Intermediated Distribution at Vero.

In a separate survey, the Insurance Council of Australia (ICA) commissioned Roy Morgan Research to ask about attitudes to flood insurance and flood mitigation.

The ICA said its survey found the “vast majority” did not support the idea of compulsory flood cover for everyone, although those surveyed were divided on whether insurers should pay claims of those who had not taken out flood cover, with 42% saying insurers should not pay these claims and 37% saying they should.

The survey found support for a ban on building in flood-prone areas, a standard definition for flood in all policies and a national database of flood risk properties.

According to the ICA, most were also in favour of State, Local and Federal governments playing a major role in protecting against floods.

“Australians understand there is no simple solution to the flood insurance debate, and we need to develop a national approach to better deal with the challenges presented by floods,” said Insurance Council CEO, Rob Whelan.

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