

INQUIRY INTO FIRE AND EMERGENCY SERVICES LEVY

Organisation: Insurance Australia Group (IAG)

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NSW LEGISLATIVE COUNCIL INQUIRY
INTO THE FIRE AND EMERGENCY
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Executive Summary

Insurance Australia Group (IAG) welcomes the opportunity to make this submission to the New South Wales Legislative Council Inquiry into the Fire and Emergency Services Levy.

Most of the funding for the New South Wales emergency services is currently provided by insurance companies, through levies on insurance policies.

Currently, uninsured properties make no direct contribution to the funding of emergency services, and the owners of underinsured properties contribute less than the owners of fully insured properties. Other States have moved away from an insurance-based funding model to property-based funding to redress inequity, improve economic efficiency and correct consumer behaviour issues posed by the underinsured and uninsured.

This submission is limited to the Inquiry Term of Reference (c) and canvasses four possible funding options for the New South Wales Fire and Emergency Services Levy. A broad-based property levy (option 3) is the preferred option as it offers the most equitable and efficient solution. Within this option there are levels of complexity for the classifications of property and use to set the levy amount. These sub-options are also considered in this submission.

IAG supports and has inputted to the submission made by the Insurance Council of Australia (ICA).

IAG

IAG is the parent company of a general insurance group (the Group) with controlled operations in Australia, New Zealand, Thailand, Vietnam and Indonesia. The Group's businesses underwrite over \$11 billion of premium per annum, selling insurance under many leading brands, including: NRMA Insurance, CGU, SGIO, SGIC, Swann Insurance and WFI (Australia); NZI, State, AML and Lumley Insurance (New Zealand); Safety and NZI (Thailand); AAA Assurance (Vietnam); and Asuransi Parolamas (Indonesia). IAG also has interests in general insurance joint ventures in Malaysia and India.

At IAG our purpose is to make your world a safer place, which means we are working to create a safer, stronger and more confident tomorrow for our customers, partners, communities, shareholders and people throughout Asia Pacific region.

Option 1 – Retain the existing approach

The current Emergency Services Levy (ESL) is a poorly targeted mechanism for distributing the cost of fire and emergency services. The system is inequitable because it fails to collect from those who are not insured or are underinsured despite both groups having equal access to New South Wales emergency services. Data shows there is no correlation between the levy amount collected and the frequency of emergency services callouts. This reflects the fact that the levy is imposed on the total insurance premium, which includes the full range of perils.

As IAG highlighted in submissions to various Federal and State Government taxation reviews, the proportion of premium attributable to each kind of risk varies considerably between postcodes, based on local factors and claims experience. At an individual household level, the premium amount, and levy amount paid, is determined by the insured value of the home and/or its contents together with other price setting factors such as loyalty and no claim discounts. This method of determining premiums means that areas with very low fire risk can contribute substantially more on a per household basis to total levy collections than other areas of the state with much higher peril risks such as bushfire or flood.

The Review of Australia's Taxation System (Henry Review) highlighted:

'Imposing specific taxes on insurance deters people from insuring their property and encourages them to bear unnecessary risks, rather than pooling risk with others. Rates of non-insurance (for building and content insurance) generally are higher at lower incomes, yet low-income people are less able to bear the risk.'

and recommended:

"All specific taxes on insurance products, including the fire services levy, should be abolished. Insurance products should be treated like most other services consumed within Australia and be subject to only one broad-based tax on consumption."

Similarly, The Report of the Australian Financial Centre Forum *Australia as a financial centre: Building on our strengths* (Johnson Report) recommended that all State taxes and levies on the insurance sector be removed as they contribute to the underinsurance problem with consequent increased demands on the public purse.

Option 2 – Introduce compulsory property insurance

Australia's home insurance market is mature and highly competitive, with a wide choice of providers and products. An essential feature of any competitive market is the choice to "opt out" of insurance altogether. While current policy settings could do more to encourage insurance, some people will always self-insure for genuine financial, cultural or philosophical reasons. This creates a powerful incentive for the insurance industry to make its products accessible and attractive to consumers.

To respond to a growing trend of non-or 'self' insurance, attract customers, and to make insurance accessible for varying customer needs, IAG's retail brands offer a broad suite of products. These provide a great deal of flexibility and choice, products include combined home and contents, prime cover home and buildings insurance and renters' insurance. Customers can choose their level of excess to reduce the amount of premium collected. Furthermore, it is easy for consumers to shop around and switch, and unlike most other financial products, contracts only run for a year with low or no exit/switching costs. These are clear advantages of the current competitive environment.

Compulsion to insure is a disadvantage as it could smother the innovation that comes with the drive for differentiation in a highly competitive insurance market. Via its retail brands, IAG is continually striving to improve the way in which we respond to each event, lifting the bar each time to surpass our competitors in terms of the quality of our disaster response and during claims time. Claims time for insurers is the moment of truth, and is arguably the most significant and critical point of contact we have with our customers.

Examples of this innovative, competitive approach include where IAG used aerial surveying overlayed with mapping software to fast-track claims following the Victorian bushfires. Also, during the Blacktown hail storms, giant crane-borne canopies were developed to allow work on roofing to continue during incessant wet weather.

Option 3 – Replace the ESL with an "across the board" property tax (which could be risked based)

A broad-based property levy is the most equitable and efficient option.

The key disadvantage of the current emergency services funding regime is that it imposes an unfair burden on people who protect their property, businesses and personal possessions by insuring them. It is their contributions that pay for the fire fighting and protection services

provided to the entire community. A fairer system would see all property owners pay for these services, spreading the burden equitably.

IAG contends that New South Wales is well placed to build on the experience of other States in relation to emergency services funding reform. The Australian Capital Territory (2006–07), Western Australia (2003), South Australia (1999), Queensland (1985) and Victoria (2013) have introduced funding systems for fire and emergency services that require property owners to contribute via a levy on property.

The main advantage of a property-based funding system is that it is broadly based, meaning that all actual and potential beneficiaries of the emergency services contribute to its funding. This eliminates the free-rider effect.

There are several potential types of property-based charges that could be considered:

'Flat' levy across all properties

The simplest approach is to apply a flat levy to all New South Wales properties regardless of value, location or use. Although relatively simple to calculate a flat levy system the main disadvantage of this approach is again inequality. Property owners paying the same levy irrespective of the value of property, use or perils risk maintains the same imbalance which exists in the current model.

'Flat' levy within sectors

A slightly more sophisticated and finely-tuned charging system would be to apply a different charge according to the type of property, but a flat charge within each property sector (e.g. residential, commercial etc).

For this type of system, it is necessary to determine what proportion of the total amount to be collected should be allocated to each sector. There are a range of possible allocation options.

The first option would be to charge the levy in line with the amount currently collected (or assumed to be collected) from each sector. A second option would be to allocate between sectors according to a measure of rateable value such as unimproved capital value or gross

rental value. For example, if the commercial sector accounts for 60% of capital value it would contribute 60% of the total funding. A flat levy would then apply to each property within the sector.

The advantages of either of these systems are:

- it is more equitable than a uniform levy for all sectors because payment is more closely related to potential benefit received from fire and emergency services; and
- it would be relatively easy to administer as there is only one rate of levy within each sector and most of the information requirements, such as capital values, are already available from Government sources.

The main disadvantage is that some relatively arbitrary judgement would still have to be made about how to charge the levy across sectors.

Differential levy system

Taking the above approach one step further, a more sophisticated and complex option would be to set different levies within sectors. Again, some decisions may need to be made about the relative proportions to be paid by each sector in aggregate.

There are a range of methods available for allocating charges between, and within sectors. The following methods are similar to those currently used in other states:

1. Allocate the charge between sectors according to their shares of a measure such as unimproved capital value or gross rental value, based on the same measure within each sector. The advantages of such a system are that it is relatively equitable in that each property holder pays according to the value of property at risk, and, that the information required is already available.
2. Allocate the charge to properties according to the type of emergency service that services that area and the level of risk for each property. This is essentially the system that is used in Queensland. The charge for residential properties varies according to the type of brigade that services that area. Charges for commercial and industrial properties are set based on the risk for each type of property.

As with the other systems, a decision must be made about the relative allocations between sectors e.g. the allocation between residential and commercial.

The advantage of this system is that it allows fine-tuning of the charges according to the potential risk for a property. It also builds into the charging structure the 'expectation of service' principle in that the residential charge varies according to which category of emergency services may attend to that property.

The main disadvantage with this approach is that it may be overly cumbersome to administer if there are many categories of property. There could also be definitional issues for some properties.

3. South Australia adopted a "hybrid" system under which funding is collected from a combination of a property based charge and a motor vehicle registration levy.

Apart from the three systems, other types of differential charging would be possible. The key decision that needs to be made is the basis for allocating the amount to be collected between and within sectors. In general, a more finely tuned system may be more equitable, but it may also be more complex to administer and may also require much more information.

User pays/cost recovery

Several of the above approaches contain elements of a user pays system, although this may not be a straightforward concept to apply to emergency services because a substantial proportion of the cost of the service is the cost of equipping and maintaining the service rather than responding to actual fires and incidents. Nevertheless, it would be possible to implement a more direct user pays system in some instances.

An obvious example of where a direct user pays approach could apply is in relation to emergency service requirements for industry, particularly hazardous materials. For example, industries that use or store hazardous materials could be required to pay a special levy or charge.

Minimising the administrative and collection costs will be important from the point of view of ensuring efficiency of any new emergency services funding system.

One option for collecting the property charge would be through a central agency such as the Office of State Revenue. The advantage of this system is that it appears to be administratively efficient. The feasibility of this approach would depend on the information used to calculate the charge (e.g. property values) being available to the central agency.

An alternative option is to collect the property charge at the Local Government level. Local Governments would need to be reimbursed for the cost of collecting the charge and the emergency services charge would need to be clearly identified on rates notices as being a State Government charge.

IAG believes Local Governments should be the preferred collection agency.

Option 4 – Funding through Consolidated Revenue

As with other services such as police and ambulance services, fire and emergency services funding could be provided from consolidated revenue, via general taxation arrangements.