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The Review Panel Members
The Natural Disaster Insurance Review
C/- The Treasury
Langton Crescent
PARKES ACT 2600

12 July 2011

Dear Sirs,

Subject - Submission to Natural Disaster Insurance Review

I have set out below a short submission to the National Disaster Insurance Review (the Review) in my personal capacity. I have been interested in the subjects being addressed by the Review for some years, principally in my former capacity as Chief Risk Officer and Chief Actuary of Insurance Australia Group (IAG) from 2000 to 2008.

I have confined my comments to three key points as I see them, as set out below:

The Review should recommend the introduction of an Automatic Flood Cover model as outlined in Chapter 2 of the issues paper dated June 2011.

The Automatic Flood Cover model proposed is, in fact, the very similar to the way home building insurance operates in New Zealand (NZ), except that there is no associated “pooling” mechanism in NZ for high risk properties. It is notable that the non-life insurance industry structure in NZ is very similar to Australia’s with the same insurance groups (e.g. IAG, Suncorp and QBE being the major non-life insurance groups in both markets). For largely historical reasons, all insurers in NZ offer flood cover as an automatic part of household buildings cover even though flood mapping in NZ is generally no better than Australia’s. This is despite flood risk in NZ being very real - there are recent examples of significant flood events leading to substantial insurance claims in NZ. Put simply, if this option works satisfactorily in NZ, as it seems to do, it is hard to see why it would not work well in Australia.

However, in the view of the writer, addition of the “pooling” mechanism for high risk properties as proposed in the Review’s discussion paper under this option (as compared to the NZ model) would create a better long term industry structure. In addition, the operation of the pooling mechanism would provide a potential source of funding for a national flood mapping authority (see below).

The alternatives set out in the discussion paper (either the “Opting Out” or the “Status Quo” models), in essence, do not really solve the major problems which caused the Review to come into existence because under those alternatives :

- (a) some people will remain uninsured against flood, and
- (b) disputes about “water damage” claims are likely to continue.

Accordingly, in the view of the writer, “the Opting Out” and “Status Quo” models are not preferred alternatives.

The Review should recommend that legal responsibility for flood mapping be removed from local Councils and given to a national authority responsible for the development and maintenance of flood maps for the whole of Australia. The authority should be obliged to make access to such flood maps freely available (via the internet). The authority could also advise on the anticipated impacts of proposed flood mitigation projects.

This will avoid the present “cottage industry” situation where some local Councils are not willing to allow flood maps to be made publically available for a range of political and legal reasons. Councils have fundamental conflicts of interest in managing this risk on an ongoing basis and are often not large enough to be able to co-ordinate flood mitigation works across boundaries between local Councils.

The proposed national flood mapping authority should also be mandated to provide mapping of properties exposed to inundation by the sea (which would mean it would need to further develop and maintain the digital terrain maps of the Australian coastline which have been created in recent years by the Department of Climate Change & Energy Efficiency (DCCEE)). This will ensure that focus is not lost on the emerging widespread risk of inundation of residential properties from the sea. DCCEE estimates that some 157,000 to 247,600 residential properties valued at some \$41 billion to \$63 billion (2008 values) are already exposed to this risk, based upon the best estimates currently available. Of these, nearly 39,000 buildings are located within 110 metres of „soft“ shorelines and are at risk from accelerated erosion due to sea-level rise and changing climate conditions.¹

The Review should recommend a level of unacceptable risk for safe building (say 1 in 25 years) at which the level of inundation risk is regarded as being simply too high to allow safe new residential or commercial development to be approved by any local or state government.

It is generally recognised that it is unwise to allow building of new properties on marginal, flood exposed, high risk land, especially where inundation is likely to destroy or substantial damage a buildings within a period that is less than the normal expected life of most buildings erected on low risk land. Nevertheless, at present, from time to time, political pressure and property development economics continue to cause such marginal, high risk land to be developed. The national flood mapping authority recommended above would be the final arbiter of whether a property has such an “unsafe for new residential or

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<http://www.climatechange.gov.au/en/publications/coastline/~media/publications/coastline/5asections511512.ashx>

commercial development” risk rating. To determine such a rating, the national flood mapping authority would be required to take an “engineering” view of risks involved at this level as an insurance market solution would not exist for such high risk properties.

This recommendation implies, as a separate matter, that the national flood mapping authority could also calibrate a lower risk “cut-off” level (say 1 in 100 year exposure) to determine the level at which the pooling of higher risk properties would operate under the Automatic Flood Cover model as proposed in the issues paper dated June 2011.

In summary, the minimum standard of (say) a 1 in 25 years flood/inundation risk for safe building could be set by legislation at a level recommended by the Review and the national flood mapping authority would then need to identify and maintain, from time to time, the list of properties that do not meet this “safe for development” standard.

Logically, this will then raise the question of what to do about existing properties that have an “unsafe for development” risk rating once they have been destroyed or substantially damaged by a natural disaster, or what the process should be if an existing owner wants to re-develop such a property before a disaster has occurred. There are a range of potential responses to this which could range from “grandfathering” existing properties to simply banning re-development of such properties so that, over time, they are likely to be destroyed and then not re-built.

In the view of the writer this would simply be another criteria added to the existing body of law and practice governing land use and planning law which determines development outcomes and the resulting ongoing valuation of individual properties.

The above discussion recognises that the insurance industry only insures the building value of properties and does not insure the land value component. In the event of a property being listed as “unsafe for development” by the national flood mapping authority the owner of the subject property is likely to suffer a reduction in the value of that property and will often seek to contest that determination.

Accordingly, in the view of the writer, the proposed national flood mapping authority will need to be structured as a statutory authority with powers and responsibilities similar to other regulators so as to make it effective.

I would be happy to elaborate on these thoughts if required.

Yours faithfully

A handwritten signature in cursive script that reads "A. M. Coleman". The signature is written in black ink and is positioned below the text "Yours faithfully".

A. M. (Tony) Coleman BA MBA Hon DBus FIA FIAA FAICD