

Manager
Cyclone Reinsurance Pool Taskforce
The Treasury
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Dear Manager

REINSURANCE POOL - CYCLONES AND RELATED FLOOD DAMAGE

Thank you for the opportunity to comment on the 'design' consultation paper for the above detailed Reinsurance Pool.

The Town congratulates the Federal Government, the insurance industry and other stakeholders, on taking a proactive role in addressing an issue that is constraining liveability and economic development in the north. While the Town is cognisant that the Northern Australia Insurance Inquiry (Insurance Inquiry) did not recommend a Reinsurance Pool because of the potential risk to Government, collectively both consultations have shed light on the gravity of insurance access, costs, and underinsurance in northern Australia and potential solutions.

During the inquiry and more recently, the Pilbara has been impacted by Tropical Cyclones Veronica and Damien and the Coral Coast by Tropic Cyclone Seroja. Anecdotally, it has been reported that some insured parties in Port Hedland have now experienced increases in premiums as a result, further entrenching the prohibitively high cost of insurance in Port Hedland, which the Insurance Inquiry found exceeded other areas in Northern Australia, notwithstanding the substantial insurance impost those areas face.

Costs in the Town have escalated markedly for small business and residents, aligned to global infrastructure stimulus packages reliant on iron ore. Employment in the iron ore industry rose by 19 percent in 2020 to just over 50,000;¹ housing sales prices have exceeded 30 percent in the last year; rents

¹ Government of Western Australia, *Western Australia Iron Ore Profile*, May 2021, p4.

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have doubled;² and construction costs are up around 160-165 against an index of 100 in Perth, with Perth construction costs much higher than Sydney.³ Further, there are \$11 billion worth in major iron ore projects currently under construction or committed to in Western Australia.⁴ In other words, lowering perennially high insurance costs for these sectors would improve affordability in a highly constrained fiscal environment.

The Town is pleased to respond to relevant questions within the consultation paper as follows, noting that some questions are best left to those with specialist insurance expertise to provide commentary.

(Question 1) How should 'cyclone' and 'cyclone-related flooding' be defined for the purposes of defining the reinsurance pool's coverage?

The Town views that the trigger definition for cyclone claims eligibility should be based on the Bureau of Meteorology's definition, the agency being the preeminent authority in Australia's weather, climate and water, including cyclone declarations, storm surge and flood forecasts. The adopted legal definition should include reference to a cyclone being declared by BoM.

A minor consideration with the BoM definition of cyclone is that infrequently a cyclone system crosses the coast and momentarily achieves Category One cyclone intensity but given relatively short duration, is managed by BoM and Hazard Management Agencies as a severe weather event as opposed to a cyclone. This could technically cause cyclone damage but is likely to only be on a relatively small scale and would be captured under storm insurance. Further, in considering an appropriate definition of a cyclone, the Town views that eligibility should not be confined to making landfall. Tropical Cyclone Veronica sat off the Pilbara coast for 24 hours and caused extensive damage to coastal infrastructure.

With respect to a definition of 'cyclone-related flooding' and the potential to extend the existing standard legal definition of flooding, the Town provides the following commentary giving regard to the two options proposed.

The Town agrees with the Taskforce regarding the complexities of determining the definition of cyclone-related flooding in accordance with flood damage occurring within a fixed proximity and time of a cyclone event. Water can continue to incur damage in the Pilbara for a substantial period-of-time (several weeks) due to hydrophobic soil or poor permeability which can

² Realestate.com, *Suburb profiles*, Port and South Hedland.

³ Regional Development Australia Pilbara, *Economic Prospects and the Cost of Doing Business in the Pilbara*, p16.

⁴ Government of Western Australia, *Western Australia Iron Ore Profile*, May 2021, p4.

cause it to pool. Also, water runoff can be exacerbated by existing waterlogged ground and flooded creeks from prior rainfall. Further, circumstances may also arise where for example, four days after a cyclone event, flooding occurs inland due to flow of river systems.

While generally agreeing with the second point pertaining to measuring the volume of rainfall brought by the cyclone that has not dispersed when flood damage occurs, the Town makes the following observations. BoM forecasts the cyclone system, storm surge and flooding (height of water) likely to be incurred or otherwise. Put simply, this is calculated by hydrologists according to a formula that accounts for soil type and dryness and predicted rainfall. Water levels in the Pilbara can be difficult to predict if there has been prior rain and water levels have not effectively dissipated for a range of reasons (i.e. exacerbation of already flooded creeks or gully collapse). Water levels therefore could be higher than BoM forecasts. So, in effect misalignment may occur between the BoM forecast water levels and the reality on the ground.

Stormwater drainage systems in Port Hedland are heavily reliant on a system of drainage channels. In the event one of those systems fails in a cyclonic event, water dissipation can be heavily impacted. The Town assumes these circumstances would be captured under the definition as engineered works which are already referenced under the standard definition of flooding and likely to translate across to a refined definition of cyclone-related flooding.

Therefore, while the Town agrees with dot point two, further consideration may need to be given to examples that apply in those circumstances so lower-level water forecasts for example do not preclude genuine damage claims.

(Question 2) Should storm surge be covered by the pool and included in a definition of 'cyclone-related flooding'?

The Town understands the following from a review of the *Northern Australia Insurance Inquiry*:

- that storm surge is captured as per cyclone under an 'other perils' component of insurance with each peril generally modelled separately in relation to expected claims, mostly based on frequency and severity models which are applied to the characteristics of the property and its location.
- that natural peril models are highly uncertain given the difficulty in assessing naturally occurring events and that the range of possible value estimates for natural peril models can be large with some values double the lowest estimates.

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- granular pricing can improve a company's risk profile for policies within its portfolio by aligning price to risk with higher premiums charged for higher risks, most likely to impact cyclone prone areas.
- some indications exist that natural peril risks may increase in the future pursuant to climate change, although it is not clear on the resultant impact on insurance premiums.
- that storm surge increases the likelihood or risk of a claim being made, particularly for home and contents insurance in a cyclone prone area.
- that some insurance companies include storm surge as a standard component of home and contents insurance and others do not.

The Town views that the complexity of calculating risk associated with storm surge; potential climate change impacts such as cyclone intensity and rate of sea level rise; coupled with offshore and onshore geomorphology for Port Hedland, warrants inclusion of storm surge in the definition of cyclone-related flooding. While Spring tidal patterns provide a level of mitigation against storm surge in Port Hedland, cyclones have occurred at high tide. The *State of the Climate Report* cites that sea level has risen faster in the north and south-east of Australia than the global average.⁵ Insured parties need to have surety around coverage for the 'suite of natural peril' risks associated with a cyclone.

(Question 3) Is it desirable for the use of standard definitions of 'cyclone' and 'cyclone-related flooding' to be required in policies covered by the pool?

The Town views that there is certainly an argument for standardisation of concepts in contracts, but it is not an expert on insurance matters and therefore is not fully cognisant of the implications of standardising definitions across insurer policies.

The Town does; however, make the following observations:

- Consistency, comparability and accountability in cyclone, cyclone-related flooding and storm surge provisions**

Standardised definitions would improve understanding, consistency and comparability for the insured and potentially the accountability of insurers, on the insurance product. The complex challenges of comprehending insurance policies were raised by the Insurance Inquiry in the following commentary:

Consumers face high costs in searching for potential alternative products, including the length of time it takes to complete online quotes, compare product features and make relevant inquiries. It

⁵ Australian Government, Bureau of Meteorology, *State of the Climate 2020*, p13.

could take a consumer over five hours to provide all the information required to obtain three online quotes and to read the full product disclosure statements for three combined home and contents insurance products.

Even if a consumer is willing to invest the time to search for alternate insurance options, the complexity and opacity of insurance markets makes it harder than it should be for consumers to understand their choices and find a suitable product. Consumers in northern Australia told us that insurance products are complex and confusing, that they lack comparability, and that pricing is not transparent.⁶

ii. Benchmarking performance of the Reinsurance Pool

Standardised definitions would likely strengthen the capacity of the Taskforce to review the performance of the Reinsurance Pool in reducing premiums and increasing access to cyclone insurance in the north. It may also assist if the Federal Government reinsures itself as the reinsurer.

iii. Cessation of the Reinsurance Pool

The Reinsurance Pool is intended to be finite, based on the concept of reduced premiums associated with increased mitigation of risk. The Town queries whether, if definitions are determined as standard definitions in insurance policies (as opposed to storm surge which is now an oncost and optional) and the Reinsurance Pool ceases, the cost of premiums will increase because those policies are all inclusive regardless of property risk via a vis that natural peril.

iv. Capacity to expand on, or amend those definitions

While hypothetical, circumstances may arise where a particular insurer does not agree with the parameters of eligibility afforded by the Reinsurance Pool and opts to extend definitions to capture additional circumstances, accepting liability or reinsuring with a provider other than the Federal Government (this is discussed under 'retention by insurers'). The Town queries whether establishing a standard definition would preclude the flexibility of an insurer to offer tailored products applying to a broader set of circumstances than afforded for reinsurance by the Federal Government? Further, whether including definitions in insurance policies would constrain the capacity of the Federal Government to amend those definitions if they are determined insufficient during the process of review of the Reinsurance Pool.

⁶ Australian Competition and Consumer Commission, *Northern Australia Insurance Inquiry final report*, p8.

(Question 4) Are there any difficulties which may arise from including home building, home contents, or residential strata policies in the reinsurance pool and how should the scope of this coverage be clarified?

i. Eligibility types

The Town makes the following comments across categories of insurance deemed eligible for the Taskforce's consideration.

The Town's Old Wedgefield Industrial area, established predominantly between the 1960s and 1980s, includes a significant number of Caretaker Dwellings. While new Caretaker Dwellings are precluded under the Town Planning Scheme (endorsed 2021), it is not clear whether the Reinsurance Pool will cover existing residences which are common in Pilbara mining towns. These dwellings are of various configurations and include separate and adjoined properties with many supporting small businesses.

Regional and rural areas have some of the highest level of disadvantage in Australia, exacerbated by a lack of access to psychosocial and medical health services and equitable levels of education.⁷ Port Hedland has a large Aboriginal population, with a chronic and preventable disease burden, and high levels of participation in the justice and child protection system. Educational attainment, although improving, is markedly lower than for non-Aboriginal people.⁸ South Hedland has a high rate of anti-social and criminal behaviour and currently a trial Banned Drinker Register is in place. Not-for-Profit (NFP) agencies are key to community wellbeing and achieving Closing the Gap outcomes. The cost of doing business in the Pilbara is extremely high and NFPs also meet a critical need where limited commercial viability exists in the provision of services (i.e. sports/childcare). While some of these NFPs will meet the definition of small businesses, various mechanisms exist for registering not-for-profits that may not be captured in this definition i.e. clubs and associations and possibly charities.

While FIFO camps are generally owned by large businesses and are not strata, smaller camps for smaller mining operations and trucking companies exist.

There needs to be some means of ensuring equity of access for small business to property insurance regardless of the configuration of occupancy, as well as

⁷ Australian Bureau of Statistics, *Socio-economic Advantage and Disadvantage*, Census 2016. Available at: <https://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/2071.0~2016~Main%20Features~Socio-Economic%20Advantage%20and%20Disadvantage~123>

⁸ Australian Bureau of Statistics, *Aboriginal and Torres Strait Islander Population – Western Australia*. Available at: <https://www.abs.gov.au/ausstats/abs@.nsf/Lookup/by%20Subject/2071.0~2016~Main%20Features~Aboriginal%20and%20Torres%20Strait%20Islander%20Population%20-%20Western%20Australia~10005>

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the capacity to limit eligibility to the determined definition of small business. If this is achieved through administrative separation of insurance components by type (i.e. small business and residential or residential and larger businesses for exclusion) then this achieves some equity. In defining costs by category of occupancy, consideration would need to be given to the impact of separating out these components in terms of risk profiling by insurers and any impact on the cost of policy premiums.

ii. Definition of small business

The definition of small business in remote mining towns is complicated by the cost of doing business and capacity to remain viable in an economy driven by extreme economic fluctuations, centred on a mono economy and predominantly iron ore. Economies of scale are incredibly important to offset high costs of transport, construction, and cost of living, and to provide salaries that can effectively compete with mining companies. Regional Development Australia produces an invaluable publication *The cost of doing business in the Pilbara* which dates from 2013 to the most recent addition in 2020. It captures the extreme cost fluctuations during the previous mining boom through the downturn. It evidences that in 2011 in Port Hedland, remuneration was 37 percent higher than Perth, housing rental accommodation 5.1 times Perth and commercial and industrial rent between 1.7 (2.9 in Karratha) and 1.5 times higher.⁹ The combined impact of costs on small business and not-for-profits resulted in Regional Development Australia Pilbara producing a *Ten Year Plan for the NGO Sector in the Pilbara* to ensure viability and maintain service capacity as well as various publications to reduce barriers to small business such as a map and gap supply chain study. In this context, the definition applied should have a higher threshold of turnover and staffing and should account for the critical role and marginal viability of NFPs in remote towns. Further, while some NFPs are part of a larger Perth-based entity, a decision to provide services in, or remain in Port Hedland, is sometimes based on cost affordability with a number electing for fly-in, fly-out, service provision.

(Questions 14 and 15) What is the appropriate level of participation in the pool, and how should considerations of coverage and the amount of risk to be ceded be addressed? / How should industry transition be managed and what is the best format and timeframe for it to take place?

There would appear to be inherent risks to Government (and insured) of non-mandatory participation in the Reinsurance Pool, specifically, achievement of the intent of the scheme in lowering premiums, warranting the cost of

⁹ Regional Development Australia Pilbara, *The cost of doing business in the Pilbara*, 2013, p4.

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administration, reliance on pooling of reinsurance funding, and reinsurance of Government as the reinsurer, if there were not economies of scale. Further, it may stymie entry of new insurers due to a monopoly on insurance supported by non-participation of insurers in the scheme and result in inequities where the Reinsurance Pool includes a power to compel in relation to price monitoring. This would be exacerbated by the fact that cyclone insurance is a soft market.

However, if it was determined that an insurer reserves the right not to participate or cede only certain components of the cyclone and related flood damage risks to the Reinsurance Pool, there needs to be transparency for the insured that their policy is not subject to the Government Reinsurance Pool. This would appear important in the context of the cost of natural perils to the bottom line of the insurance companies and the Government guarantee.

If participation is deemed mandatory which seems appropriate, then a standard assessment of risk as a trigger for participation should apply. In Western Australia, this could be informed by requirements under the State Planning Policy No.2.6: State Coastal Planning Policy in combination with other relevant hazard planning for cyclones.

(Question 16) What should be the key goals for a regular review of the reinsurance pool and what would be the optimal timeframe?

The Town is of the view that there needs to be an interim review within 12 months of the establishment of the Reinsurance Pool to ensure early evaluation and remediation of issues and potentially within a specified timeframe following a catastrophic cyclonic event. Other regular reviews to be determined as required. The scope of those reviews may vary to ensure appropriate use of resourcing.

The indicators of success are appropriate, but government may also wish to consider:

- the performance of the definitions/concepts in capturing claims following a cyclone/storm surge event (if feasible);
- whether the Reinsurance Pool has incentivised new entrants into the cyclone-related insurance market, particularly given reports of an insurance monopoly in Northern Australia.¹⁰ Entry of new players will be important for market competitiveness during the period of the Reinsurance Pool but also as a means of determining whether the

¹⁰ Australian Senate, *Northern Australia Agenda Select Committee, Hansard*, 12 March 2021, p12.

Reinsurance Pool and associated focus on mitigation results in a sustainable easing of the insurance burden.

- whether insurance premiums have been impacted by community mitigation and planning controls; and
- making commentary about further opportunities for reducing premiums within the Government policy environment i.e. planning and development controls, improvements to the Building Code, Government subsidisation initiatives for private property mitigation, etc

(Question 17) Should the reinsurance pool have a planned exit date?

An indicative exit date may be applicable, but the Town respectfully suggests that it is contingent on:

- performance of the Reinsurance Pool as a mechanism for reducing premiums and whether that result is sustainable in the absence of the Reinsurance Pool; and
- financial risk to government.

(Question 18) Which mechanisms will ensure the pass-through of reinsurance premium savings to insurance policyholders?

As a general premise, the Town supports greater accountability and transparency in the expenditure of Government funds for the insured, and to facilitate efficacy in the review of the Reinsurance Pool through provision of accurate data.

(Questions 19 and 20) To what extent do insurers price in discounts into insurance premiums for mitigation action undertaken by or affecting policyholders?/How might mitigation be encouraged by the reinsurance pool's design?

The Town views that encouraging the concept of owner mitigation is positive, particularly against cyclone wind and rain damage; however, is more complicated in terms of cyclone-related flooding and storm surge. It appears however, that there is currently a narrow margin for cyclone insurers, so it is not clear how much of a discount can be afforded.

The other issue for remote towns is that the cost of undertaking these works (as indicated by some of the data above and the requirement to meet cyclone code) can be extremely expensive and cost preclusive, hence consideration may need to be given to government subsidies being applied for older properties.

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The Reinsurance Pool may also provide an opportunity for education on mitigation through policies to policy holders.

(Question 21) How should the pool's design seek to discourage any increase in risky behaviour? (Should there be a time-based cut-off to exempt new builds from the pool?/Should the pool only allow new builds that have been built to adequate standards and in suitable locations?)

The issue of construction of housing in high-risk areas is more relevant to State and local government planning controls. In Western Australia, the State Coastal Planning Policy requires the preparation of a detailed Coastal Hazard Risk Management and Adaptation Plan for coastal towns which reviews storm surge and inundation in accordance with prescribed guidelines. Local Planning Frameworks are required to reflect the policy and in the case of Port Hedland, the Town has introduced provisions in their Local Planning Scheme and prepared a draft Local Planning Policy: Coastal Planning to:

- avoid inappropriate land use and development of land at risk from coastal erosion and inundation.
- ensure that land use and development considers coastal processes within the 100-year coastal planning horizon and applies appropriate measures.
- establish appropriate instruments for disclosing to those likely to be affected, where a coastal hazard risk has been identified or where development is subject to a limited approval.
- ensure land in the coastal zone is continuously provided for coastal foreshore management, public access, recreation and conservation.

The draft policy is due to go to the Council and is available on request.

Mining Towns in the Pilbara are in the grip of a housing crisis and to further constrain economic development and liveability by refusing access to the Reinsurance Pool would be counterintuitive. The Town supports the Reinsurance Pool extending to new properties compliant with the Building Code and land use planning and development controls. The Town views that it is more appropriate that properties be insured than uninsured or underinsured. Insurance is a legal requirement under mortgage contracts and commentary to the Select Committee on Northern Australia labelled insurance as an 'essential service'.¹¹ One of the issues for remote towns in northern Australia is how economic development is achieved without adequate access to insurance coverage, in circumstances where there is a defined market failure.

¹¹ Ibid., p34.

For new properties, reference to the Reinsurance Pool only applying where the Code and Standards 'adequately mitigate cyclone and flood damage risk' needs to be qualified as it could result in discretion as to what constitutes 'adequate'. Construction in a 'suitable location' while unqualified is also problematic. In Port Hedland, land is at a premium and urban sprawl is not an option given Native Title considerations and the Port is in Port Hedland which is separated by an 18km causeway to South Hedland. New property construction in Port Hedland is required to be effectively above the forecast flood line, accounting for predicted sea level rise. Builds are required to be cyclone coded Category D as per the Building Code.

(Question 22) To encourage further action by states and territories on insurance affordability (What settings could be included in the design of the pool?/Which policy options could be introduced alongside the pool?)

Realistically, there needs to be a whole of government response to mitigation, including around climate change impacts. The Town has experienced significant difficulty in accessing funding for seawalls identified through conduct of its Coastal Hazard Risk Management and Adaptation Plan and coastal engineering studies.

The Town also views that insurance companies should be compelled to share aggregate information with State and Local Governments to help improve local planning and building regulations.

The Town has previously called on the State Government to abolish State taxes on insurance (and GST on the total premium) to alleviate the cost burden on the insured of high-cost premiums. This was the intent of the ACCC inquiry.

The Town supported directing a portion of stamp duty revenues to affordability measures for low-income insurers. There may also be scope for investing in Town-based mitigation measures. Evidence to the Senate Select Committee on Northern Australia earlier this year highlighted the success of community mitigation measures in Roma on reducing premiums.¹² Community mitigation is important but adequate access to government grants is required and issues of transfer of liability for property damage resulting from community mitigation needs to be considered.

The evidence to the Senate also centred on increasing Building Code standards. As noted, the cost of construction in northern towns is extremely high due to factors previously mentioned coupled with compliance with the cyclone code. While protection of life is paramount, there needs to be a

¹² Ibid., pp26-27.

balance between affordability and securing protection of goods and chattels from cyclone-related flooding and storm surge.

Should you require further information to support the submission, then please contact [REDACTED]

The Town appreciates the opportunity to comment.

Yours sincerely



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18 June 2021

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