2 July 2024

Select Committee on the Impact of Climate Risk on Insurance Premiums and Availability
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Dear Secretary,

Introduction

Strata Community Association (Queensland) "SCAQ" is the peak association supporting Queensland's strata sector, with more than 1,300 individual and corporate members who help oversee, advise and manage assets worth some $280 billion on behalf of homeowners and investor owners. As the peak body for the strata industry, SCAQ is in the unique position to understand the sector from all angles.

SCAQ is in an enviable position to understand the sector from a broad array of viewpoints owing to its diverse membership. SCAQ represents strata managers and service providers, meaning we can advocate from a "whole of industry" perspective.

SCAQ proudly fulfils the dual roles of a professional institute and advocate for our members' consumer clients.

There are over 53,000 community titles schemes and over 540,000 individual lots in Queensland. Lot owners are part of the body corporate, and a committee is responsible for the day-to-day management of the scheme, such as maintaining common property. Under body corporate legislation, a tenant is known as an 'occupier' and occupiers have significant rights and responsibilities in relation to the body corporate.

We are also a constituent of Strata Community Australasia (SCA), the peak industry body for Body Corporate and Community Title Management (also referred to as Strata Management, Strata Title or Owners Corporations Management) in Australia and New Zealand.

Policy Submission

Submission to the Select Committee on the Impact of Climate Risk on Insurance Premiums and Availability

In 2012 SCAQ, jointly with our colleagues at SCA, was the first organisation to publicly advocate for the establishment of a Cyclone Reinsurance Pool to support property owners in Far North Queensland. This finally became a reality in 2022 in one of the few positive developments in that market since that time.

In 2021 we released an industry-first report highlighting the spiraling costs of strata insurance and the high burden of government taxes, duties and levies, adding on average 27.5 per cent to premiums across Australia and up to 40 per cent when NSW's emergency services levy is included.

In Northern Australia, affordability pressures are difficult, with some strata communities struggling to find available policies. Caused identified included reinsurance market costs, global climatic events, Australian climatic events, building defects and cladding risks.

The report documented the role and value of the strata manager of navigating the complexity of the insurance process on behalf of strata owners, identifying 47 separate pieces of work related to obtaining suitable cover, keeping records, providing advice and managing claims.

Strata managers sit in the middle of a complex web, providing value to strata communities, brokers, insurers, underwriters and suppliers through their knowledge of the specific strata community, the relevant legislation and regulations and their duty to act in the strata community's best interests.

Against this background, the Senate Select Committee is a welcomed and timely opportunity to return the focus to the needs of strata owners who face ongoing challenges with affordability, and in certain instances availability, of insurance. These are largely unchanged since our landmark report in 2021 and in some respects they have become worse.

This submission responds to the Terms of Reference as they relate to the current situation in Queensland, and particularly Far North Queensland. Strata insurance is a national market and many of the issues raised here will be common to all jurisdictions.

(1) the unaffordability of insurance in some regions due to climate-driven disasters;

Member feedback is that the introduction of the Cyclone Reinsurance Pool is beginning to have some impact on premiums in Far North Queensland, but the evidence is patchy and inconsistent across insurers, brokers, locations and property types. There has been no significant improvement in competition, and it is rare to be able to obtain more than one quote on any particular property - let alone the three quotes considered best practice in the rest of Australia.

Typical recent examples:

- A 35 year old, 8-unit apartment block in a well-protected area of Cairns with no claims history and a $2.5 million replacement value did receive two quotes. One was $13,851, the other $45,650.
- A 6-lot, fully owner-occupied light industrial site with a $3.5 million replacement value could only obtain one quote at $29,230.

In general, the only competition seen is for these types of smaller risks. We understand that one insurer is starting to provide more quotes and the launch of an additional insurer in 2019 did increase the number of options available for obtaining quotes.

SCAQ also understands that an insurer has recently announced an increase in their risk ceiling to properties with a replacement value of up to $20 million – we understand it is currently $5 million – but this is yet to take effect.

For larger schemes with higher replacement values, or those with mixed residential and commercial tenancies, quotes are difficult to find at any price.

- A 19-unit waterfront residential complex (replacement $24m) with no claims from the most recent cyclone Jasper had no option but to renew at the only quote available of about $260,000 or more than $13,500 per owner.

Where quotes can be obtained, there is little consistency, and the outcome is unpredictable and difficult to budget for. This presents its own challenges in terms of planning for maintenance or remedial works that might make a building more resilient to climate-related weather events.

(2) the unavailability of insurance for some people due to climate-driven disasters;

Strata insurance is compulsory in all states and territories. This should ensure universal coverage in theory, but in practice aggressive risk avoidance by insurance underwriters makes it difficult for some schemes to obtain cover at all. In Far North Queensland this is a common scenario and, anecdotally, it is increasing in other parts of Australia.

This leaves owners very exposed to climate-related weather events. For investors and their lenders, it puts their capital at risk while for residents it can mean the loss of their homes.

States, generally, do not actively police compliance with compulsory insurance. Amendments to Queensland legislation in 2023 created a pathway for approval of an "alternative insurance" scheme. But the cost of insurance alone is not sufficient grounds for approval and we are aware of only one active application. We are also aware of several more properties that have chosen to fully self-insure by agreement among the owners, something also not legally permitted under this pathway.

One problem for the Select Committee to consider is the lack of empirical data to measure how widespread this problem is, and how that information might be collected. Otherwise, the full extent may only become apparent at the next major weather event.

One aspect that should be quantifiable is the growing use of excesses, which have partially offset the direct impact of premium increases. Increasingly, we are seeing higher excesses imposed without any corresponding premium reductions. Minimum excesses of $2000-5000 are now standard in Far North Queensland, rising to $10,000 for water damage claims and $50,000 for cyclones. In the most recent major event, Cyclone Jasper, our members reported seeing very few water damage claims because the impact on most of their clients did not reach the excess thresholds.

There is an open question as to whether excesses of such magnitude are consistent with the legal requirement of compulsory insurance for the full replacement value of the property. This has not yet been tested in any court of record that we are aware of. In our view the time is approaching where regulators will need to draw a line on what is an acceptable level of dilution of statutory obligations.

(3) the underlying causes and impacts of increases in insurance premiums;

It is not disputed that the effects of climate changes on the severity and frequency of major weather events are impacting the cost of insurance globally. The major increases in premiums being seen in Australia across the board, and most acutely in Far North Queensland, reflect this long-term trend.

That said, other factors have compounded the impact of the global climate trend, including:

- An epidemic of construction defects, most commonly waterproofing and non-compliant cladding, that increase the probability and cost of severe weather damage.
- Widespread shortfalls in maintenance and repair of common property, which also increases risks associated with weather events. Ironically, this is partly attributable to the pressure on owners corporations budgets from escalation of mandatory insurance premiums, reducing the capacity of owners to fund discretionary but essential maintenance.
- Excessive government taxation with state duties and levies on top of GST compounding the rises in underlying premiums.
- A highly concentrated insurance market with limited competition and choice.

(4) **the extent to which increased climate risk is being priced into insurance products not exposed to climate-driven risks;**

The lack of available data on strata claims makes it impossible to quantify the contribution of climate risk to the growth in premiums. We understand the insurance industry has a data clearing house for other property insurance classes which enables in-depth independent analysis. The lack of an equivalent data repository for strata insurance is a significant gap in our understanding of the exposure of Australians to climate risk and something we would urge the Select Committee to address in its report.

(5) the distributional impact of increases in insurance premiums across communities, demographics and regions

The gap in data on strata insurance costs also makes it difficult to understand how premium increases are being distributed. Far North Queensland has experienced premium increases of a different magnitude and for a longer period than the rest of Australia. But there is no independent, objective analysis that would tell us the extent to which this is justified by underlying claims and reinsurance costs or influenced by other factors, such as the lack of competition in that market

(6) the role of governments to implement climate adaptation and resilience measures to reduce risks and the cost of insurance;

Rising insurance premiums, in a perfect market, should prompt more investment in improving resilience to weather events that would result in reduced premiums. We are aware of instances where substantial investments in flood mitigation for large, high-value riverfront properties in Brisbane have resulted in substantial reductions in premiums.

But these are exceptions and strata insurance is not a perfect market, not least because governments have made it compulsory. In practice, for the more exposed strata communities in particular, the crippling cost of insurance renders it very challenging to raise the funds needed to fully comply with their other statutory obligations to repair and maintain common property. Raising further large amounts from owners to invest in resilience measures would make those choices only that much harder. Securing owners' agreement to contribute those funds is all the more difficult when there is no guarantee of any reduction in premium on the other side.

Some limited steps have been taken by governments to provide grant support and other incentives to invest in resilience. These are welcome but only a start. Much more is needed, including measures to incentivise insurers to contribute more certainty to the business case for owners' investment in terms of a reduction in premium.

(7) how the pricing of risk from climate-driven disasters can be better redistributed across the economy; and

Better data and independent analysis, as identified in our responses to **(d)** and **(e)** above, should be the starting point for understanding the current dynamics around the distribution of risks from climate-driven disasters.

In principle, insurance plays an important role in providing price signals around risk and encouraging measures to reduce risk. But that assumes a well-functioning market where there are competitive tensions and informational symmetries that provide checks and balances to ensure that differences in premiums are proportional to differences in risk.

As noted earlier, strata insurance falls short of a well-functioning market in many respects, particularly but not exclusively in Far North Queensland. The Cyclone Reinsurance Pool is an important step towards smoothing premium volatility and improving the credibility of insurance price signals. But more needs to be done, starting with better collection of data

(8) any other related matters

This Select Committee is inquiring into a key point of intersection between the three defining policy challenges of our time – climate change, the rising cost of living and housing access and affordability. It is therefore important that its report and recommendations reflect a holistic view through all three of those lenses.

SCAQ agrees that there is a fundamental relationship between the cost of insurance and the risks associated with climate change.

But insurance price signals need to be equitable and proportional to differentials in relative risk. We do not believe that the current market is operating efficiently, with the burden falling disproportionally on specific groups because of housing choices made in good faith and in most cases long before the current market drivers became apparent.

Insurer risk-avoidance is the major contributor to the creation of a whole class of home owners and housing investors who are trapped in a spiral of rising occupancy costs and stagnant or declining property values. This is the norm in Far North Queensland, and increasingly so elsewhere in Australia because of the increase of construction defects in buildings.

Under any scenario for an effective response to Australia's chronic housing shortages, strata-type developments will play a key role in delivering more choice and greater affordability. However, the perfect storm of rising construction costs and rising ongoing costs, mainly driven by insurance, has stalled the private market's response to the pent-up demand. In Cairns, this otherwise dynamic regional centre has seen no new private medium density housing development for more than a decade. It has an average rental vacancy rate of 0.4 per cent.

SCAQ is playing its part in building confidence in strata living for owners and residents with its professional development programs to upskill and expand a growing strata management and strata services sector. However, the need for building confidence goes far beyond the areas within our direct control. It needs leadership from all levels of government and all service sectors, including in the strata insurance market.

Kind regards

Laura Bos
General Manager, SCAQ