

8 June 2012

Ms R Sadlier
New Zealand Productivity Commission
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By email: transtasmanreview@productivity.govt.nz

Dear Robyn

STRENGTHENING ECONOMIC RELATIONS BETWEEN AUSTRALIA AND NEW ZEALAND

The Insurance Council of New Zealand ("the Insurance Council") appreciates the opportunity to comment on the Australian and New Zealand Productivity Commissions' Issues Paper "Strengthening economic relations between Australia and New Zealand".

1. Insurance Council

The Insurance Council is the industry representation body for fire and general insurance in New Zealand. The Insurance Council has 26 members which write the substantial majority of New Zealand's insurance business.

The Insurance Council is active in self-regulating the insurance industry. We promote the Fair Insurance Code that requires Insurers to act ethically. We fund the Insurance & Savings Ombudsman Scheme that offers independent review of decisions and we apply an Insurance Council solvency test that confirms the financial stability of our members. We also require members to be independently rated and to publish these ratings. We perform an important role in informing and educating consumers about key insurance issues and risks.

A number of our members are part of groups which operate in both Australia and New Zealand. Accordingly, the Insurance Council supports initiatives that help harmonise regulation, where appropriate, and that drive economic growth. Nevertheless, it is imperative that differences in size and scope between the two markets are understood and appreciated when looking at harmonisation.

2. Regulatory Harmonisation

There are significant differences between the current insurance markets and regulatory regimes of New Zealand and Australia. Each country has distinct markets and products, meaning Australian systems cannot simply be transplanted directly into New Zealand. If the two respective Governments are seriously considering integrating New Zealand and Australia's insurance markets, they need to completely rethink the regulatory differences, particularly with respect to material differences in underlying liabilities (and the consequential changes in reserving practices) and licensing requirements.

Nevertheless, it needs to be noted that there are substantial differences in market size and scope between the two countries, meaning Australian regulations and market conditions may not be workable, or even appropriate, in New Zealand.

3. Liability Differences

The law within Australia is not consistent between states and territories and again between those jurisdictions and at the Federal level. This can be seen, for example, in the way taxes and levies are imposed as well as the way personal injuries are assessed and compensated. There are also differences in liability thresholds and ranges of compensation for what may seem to be similar events. These differences lead to changes in how capital is reserved and managed.

Serious consideration is required to fully appreciate what it is that is classified as “Australian” and alongside which New Zealand is expected to be consistent. Certainty is needed to ensure longer term investment and lower friction, and to allow more open and smooth operations on a trans-Tasman basis.

4. Solvency Standards

The Insurance Council appreciates moves by the Reserve Bank of New Zealand to harmonise certain regulatory developments with those of the Australian Prudential Regulation Authority (“APRA”). Nevertheless, there is one particular area we believe has not been given effective consideration by the current Government.

New Zealand’s proposed solvency requirements are completely out of synchronisation with Australia. The Insurance Council remains concerned with the level of capital required under the proposed New Zealand standard in comparison to the Australian APRA requirements. The difference in catastrophe risk profile between New Zealand and Australia is certainly not so great so as to justify such a significantly different solvency requirement (Australia is currently required to purchase sufficient reinsurance to cover each 1 in 250 year event, whereas New Zealand is required to purchase sufficient reinsurance to cover each 1 in 1000 year event).

We agree with the Insurance Council of Australia in that such stringent requirements will only serve to impede international competitiveness. Higher capital requirements will likely discourage investment in New Zealand and be a significant barrier to entry to the New Zealand market. The proposed 1:1000 requirement will make New Zealand a much less attractive place for international insurers to do business and will negatively impede the affordability and availability of insurance for all New Zealanders, inevitably placing greater burden on the state in the event of disaster.

5. Broker Regulation

There is also a serious liability mismatch between New Zealand and Australia with respect to regulation of insurance brokers. For example, New Zealand does not require any remuneration disclosure by insurance brokers, in complete contrast to the Australian regime. The Insurance Council is concerned that not requiring disclosure of remuneration may have the following negative impacts on New Zealand’s insurance industry:

- continued lack of transparency for consumers regarding the real cost of insurance;

- no real incentive for brokers to ensure their recommendations are based on the client's best interest, rather than based on the level of commissions received by the broker; and
- falling short of best international practice.

For the benefits of market integration and enhanced transparency we would suggest that New Zealand looks to develop similar compulsory disclosure requirements to Australia. Disclosure of remuneration would provide a higher level of transparency and allow customers to be aware of the level of fees and commissions they are paying and, as a result, make better and more informed decisions.

6. Taxation/Levies

It is also imperative to have reductions in some of the current general levies and taxation placed on insurers (i.e. the fire service levy and the earthquake levy) to ensure that insurance remains affordable and available for a significant proportion of New Zealanders. Otherwise, New Zealand again risks falling behind Australia. Costs for the fire service levy for example should correspond with property rates or general taxation, rather than insurance (a shift of burden which has been recognised within Australia). Otherwise those with insurance are effectively cross-subsidising those without. This point has been raised repeatedly with the Ministry for Internal Affairs, to no avail, and is an example of where New Zealand is lagging behind Australia in regulatory development. Compliance costs are directly causing increases in insurance costs and so long as these costs continue there will be significant problems with under and non-insurance in New Zealand.

7. Conclusion

Thank you again for the opportunity to provide input on the Issues Paper. The proposals are of significant interest to our members.

We appreciate that this proposal is very much in its early stages; nevertheless, we would be very interested in discussing the issues raised in our submission in more depth and/or arranging a meeting between the Productivity Commission and our Regulatory Committee.

Yours sincerely

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