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Insurance Australia Group (**IAG**)[1] welcomes the opportunity to make a submission to New South Wales (NSW) Review of Federal Financial Relations *Discussion Paper – Working together for a better future.*

With more than 8.5 million customers and information on the majority of motor vehicles and domestic residences in our markets, we use our leadership position to understand and provide world-leading customer experiences, making communities safer and more resilient for the future. Our purpose is to make your world a safer place. We recognise that our role extends beyond transferring risk and paying claims. Our purpose drives our business to work collaboratively with the community to understand, reduce and avoid risk, and to build resilience and preparedness.

IAG has been a strong advocate for improved taxation bases and taxation reform that see revenue dependency shift from transaction style taxes (for example insurance) towards those taxes that are more efficient.

IAG believes the current regimes for the taxation of insurance are inconsistent upon the generally accepted taxation principles of simplicity, efficiency and equity. These tax regimes are inappropriate, regressive and based on historical circumstances rather than equity.

IAG notes the *Discussion Paper – Working together for a better future* (October 2019) examines how NSW and the Commonwealth can work together to build a stronger economy, encourage state-led reform, and ultimately, deliver better value for taxpayers. The *Discussion Paper* notes:

"Insurance based taxes (insurance duty, emergency services levy contribution, health insurance levy) are commonly considered to be one of the more costly taxes to society. By adding to the price of insurance, they can result in underinsurance and non-insurance."

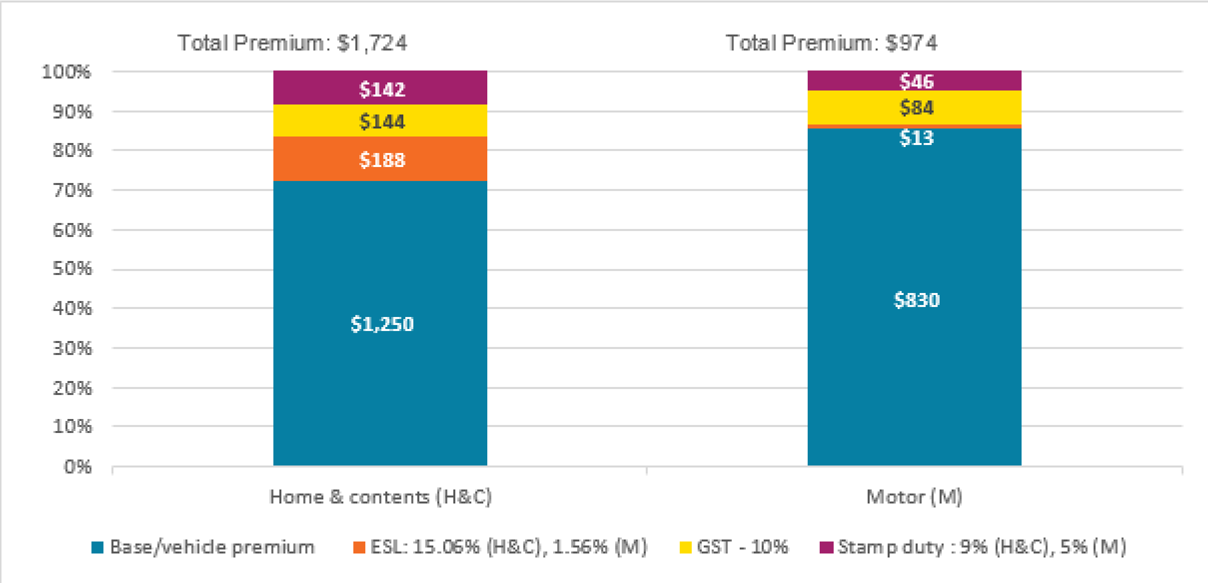
Impact of State Insurance Taxes on Insurance Premiums

State insurance taxes in NSW represent a significant portion of the cost of home, strata and car insurance premiums. The following is a graphical representation of the example home & contents

[1] IAG is the parent company of a general insurance group with controlled operations in Australia and New Zealand. Our 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 (in Australia); and NZI, State, AMI and Lumley Insurance (in New Zealand).

and motor insurance policies highlighting the impact of insurance taxes on insurance premiums.

Table 1: Premium components by category



Source: NSWESL Monitor https://www.eslinsurancemonitor.nsw.gov.au/understanding-your-premium

Possible Emergency Services Funding Reform

Option 1: Replace the Emergency Services Levy (ESL) with an "across the board" property tax

NSW is the only State on mainland Australia that retains an insurance-based funding model for the provision of fire and emergency services. Queensland and South Australia moved to a property-based funding model in 1984 and 1999 respectively. Western Australia moved to a property-based funding model in 2003, while Victoria moved to a property-based funding model in 2013.

Several Government inquires, and reviews have concluded that funding emergency services through an insurance levy is inefficient and unfair. For example, the 2004 New South Wales Public Accounts Committee Review of Fire Services Funding; IPART's 2008 Review of State Taxation; the 2009 Henry Tax Review; and the 2009 Victorian Bushfires Royal Commission.

The current 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 NSW 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 has 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.

Moreover, the current funding model is overly complicated and confusing for three main reasons:
1. Insurers are not aware of their final ESL obligations to the NSW Government until after they have collected the ESL from their customers.
2. Insurers are required to use a model to estimate several inputs, including forecast premium data and total market premium pool size, to estimate their share of the total budget of the NSW Fire and Emergency Services authorities.
3. The ESL charged on insurance funds fire and emergency services for the financial year in which the policy commenced rather than for the policy term of the insurance policy. This often results in confusion for customers.

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.

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 NSW is well placed to build on the experience of other States in relation to emergency services funding reform that have introduced funding systems for fire and emergency services that require property owners to contribute via a levy on property.

IAG believes that a property-based levy is a fairer, simpler and more sustainable approach to funding fire and emergency services. The change will be fairer for our community as these important services will now be funded by all property owners, not just those with insurance. Removal of the ESL on insurance will also see savings in insurance premiums passed on to customers. This is an important first step in addressing insurance affordability, accessibility and participation.

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.

Option 2: Funding Emergency Services 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.

Possible Insurance Stamp Duty Reform

Several Government reviews and inquiries have advocated for the removal of stamp duty on insurance contracts. For example, the Review of Australia's Future Tax System recommended "all specific taxes on insurance products, including the fire services levy, should be abolished." Similarly, the Australian Competition and Consumer Commission's (ACCC) *First Interim Report*, Northern Australia Insurance Inquiry 2019 stated "It has been widely acknowledged that stamp duties on insurance contracts are an inefficient form of taxation." The ACCC recommended stamp duty on home, contents and strata insurance products be abolished.

The ACCC's *Report* also noted:
"In October 2015 the ICA commissioned Deloitte Access Economics to write a report on the impact of removing stamp duty from insurance around Australia, and replacing the lost revenue with an increase in municipal land rates. The report found that removing all insurance-based stamp duties across Australia, including the Emergency Services Levy in NSW, and replacing them with commensurate increases in municipal land rates, would lead to a net increase in real private consumption across Australia of $5.52 billion, and a net increase in tax revenue collected by state and local governments of 0.69 per cent. These figures relate to a broad range of insurance products, not just home, contents and strata."

IAG believes the removal of all State Government taxes and duties on general insurance products is an important first step in addressing insurance affordability, accessibility and participation. IAG argues that there is a clear social and economic case for eliminating or at least reducing State insurance taxes. This case is based on recognition of the essential benefits of insurance to the economy and community generally and of the role of the tax system in encouraging insurance coverage.

If you have any questions or require any further information please do not hesitate to contact David Wellfare, Executive Manager, Public Policy & Industry Affairs on (02) 9292 8593 or David.Wellfare@iag.com.au

Yours sincerely

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