



THE LAW SOCIETY
OF NEW SOUTH WALES

Our ref: BLC:BMsh120824

12 August 2024

Dr James Popple
Chief Executive Officer
Law Council of Australia
PO Box 5350
Braddon ACT 2612

By email: Ashna.Taneja@lawcouncil.au

Dear Dr Popple,

Impact of Climate Risk on Insurance Premiums and Availability

The Law Society appreciates the opportunity to provide input to a Law Council submission to the Senate Select Committee on the Impact of Climate Risk on Insurance Premiums and Availability. We note the Select Committee has called for submissions detailing challenges with insurance affordability including the availability of insurance for those living in regions impacted by climate-driven disasters. Our Business Law Committee contributed to this submission.

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

Our members are aware of instances of small businesses experiencing difficulty obtaining insurance due to significant increases in premiums. This is particularly acute for those that are more vulnerable to climate change risks, for example in relation to flood cover in various parts of the Mid-North Coast region of NSW. We understand that small business insurance premiums have regularly risen in recent years, with the increasing frequency and intensity of natural disasters identified as a significant driver of this upsurge.

Locations suffering extreme insurance affordability pressures are concentrated in disaster-prone regional areas.¹ We also note commentary that states “there is no clear data about the nature and scale of non-insurance and underinsurance due to unaffordable premiums”.² We suggest this creates significant risks in terms of predicting the potential economic impact of climate related natural disasters, and likely reliance on post-disaster government assistance by the uninsured.

¹ Actuaries Institute, *Home Insurance Affordability Update Report*, August 2023, 13, https://actuaries.asn.au/docs/thought-leadership-reports/home-insurance-affordability-update.pdf.pdf?sfvrsn=7737bcf4_4.

² CHOICE, *Weathering the Storm: Insurance in a changing climate*, August 2023, 16, <https://www.choice.com.au/consumer-advocacy/policy/policy-submissions/2023/august/climate-insurance-report-Weathering-the-storm:Insurance-in-a-climate-crisis|CHOICE>.

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

Self-evidently, increasing premiums reduce the availability of insurance, particularly for small business. We also understand that coverage for certain lines of insurance is being withdrawn completely. For instance, we note that fewer policies are available in regions more vulnerable to worsening climate change impacts, because of risk management mechanisms such as exposure limits (designed to cap the volume of customers or proportion of sums insured) and embargoes (applied to deny underwriting policies entirely) implemented by insurers to avoid potentially significant claim costs.³

We note that comprehensive insurance coverage for climate perils can play a critical role in absorbing the costs of future climate damages and losses and in supporting economic recovery in the aftermath of these events:

There is some evidence that higher levels of insurance coverage for damages and losses from disasters is linked to quicker recovery and more limited economic disruption.⁴

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

Increases in premiums are recognised as predominantly caused by a hardening of the market with insurers seeking to recover record losses from significant disaster events in recent years. A major contributing factor is higher building replacement costs, due to continuing materials and labour shortages driven by disruptions to global supply chains. This, in turn, leads to higher homeowner and commercial property claims.

Risk modelling methodology has also been reported as an emerging factor contributing to increases in insurance premiums.⁵ The unpredictability of climate-driven catastrophic events has made it challenging for insurers to accurately price risk. However, understanding of risk is evolving, with the use of new and emerging technologies for catastrophe modelling which has led to higher resolution data at the residential address level. Insurers have acknowledged that,

more granular risk modelling has resulted in changes to premiums at a policy level, with some consumers in higher-risk areas seeing premiums increase and others in lower-risk areas paying less for their premiums.⁶

We note that risk analytics and modelling expertise developed by insurers to manage their own exposure could be utilised to reduce costs for policy holders in high-risk areas, by encouraging mitigation to lower their risk.

(d) the extent to which increased climate risk is being priced into insurance products not exposed to climate driven risks

We understand this term of reference to be related to the principle of cost-sharing where risk is spread across a broad base of policyholders so that low risk customers are charged higher premiums to cross-subsidise high risk customers. There is substantial commentary on cross-subsidisation as a mechanism to improve affordability and there are a diversity of views on its

³ ACCC, *Insurance monitoring - Second report following the introduction of a cyclone and cyclone-related flood damage reinsurance pool*, December 2023, 73 -74, <https://www.accc.gov.au/system/files/accc-insurance-monitoring-report-december-2023.pdf>.

⁴ Organisation for Economic Cooperation and Development, *Enhancing the insurance sector's contribution to climate adaptation*, Policy Paper, March 2023, 4-5, https://www.oecd.org/en/publications/enhancing-the-insurance-sector-s-contribution-to-climate-adaptation_0951dfcd-en.html.

⁵ n 3, 47.

⁶ Ibid.

effectiveness and fairness.⁷ Also, as previously discussed, the increased refinement of risk-rating is recognised as leading to an unwinding of cross-subsidisation methods.⁸ The data analytics and methodologies used in assessing risk and applying ratings is highly complex and evolving. In our view, confidence in the equitable setting of premiums would be improved with information transparency, education and oversight of new and emerging approaches to use of data and pricing. Open access to climate risk data may also enhance climate adaptation in the long term.⁹

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

Further to the discussion under (b) above regarding the disproportionate impact of climate change on regional communities, we also note that lower uptake of insurance has been associated with a lower socio-economic profile and/or higher exposure to extreme weather.¹⁰ Low insurance literacy is another contributing factor to non-insurance and under-insurance and varies geographically with lowest literacy in more remote areas. There is a compounding effect with many who do not have coverage viewing insurers as untrustworthy based on dissatisfaction with previous claims experience.¹¹

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

The role of governments in land use and planning is important in mitigating climate-related risks, and hence assist in achieving affordable premiums. In the NSW context, the Law Society has previously advocated for a whole of government approach to climate change, which requires emissions reduction targets set by the State Government to be enshrined in a legislative framework, now introduced with the enactment of the *Climate Change (Net Zero Future) Act 2023* (NSW) and, crucially, the integration of climate change into the NSW planning system.¹²

⁷ See for example: Actuaries Institute, n 1, 22-27; ACCC, n 3, 13-14, and Productivity Commission, *5-year Productivity Inquiry: Managing the climate transition Inquiry report – volume 6*, 2023, 5-8

⁸ See also Finance and Public Administration References Committee, Parliament of Australia, *Lessons to be learned in relation to the Australian bushfire season 2019-20 Final Report*, 2021, 79, https://parlinfo.aph.gov.au/parlInfo/download/committees/reportsen/024627/toc_pdf/LessonstobelearnedinrelationtotheAustralianbushfireseason2019-20-FinalReport.pdf;fileType=application%2Fpdf

⁹ n 4, 11-13.

¹⁰ Actuaries Institute, *Home insurance affordability and socioeconomic equity in a changing climate - Green Paper*, August 2022, 17-18

<https://www.actuaries.asn.au/Library/Opinion/Generalinsurance/2022/HIAGreenPaper.pdf>.

¹¹ Ibid.

¹² See Law Society of NSW, [Inquiry into the planning system and the impacts of climate change on the environment and communities](#), 3 November 2023, Law Society of NSW, [EPA Climate Change Policy and Action Plan](#), 4 November 2022, and Law Society of NSW, [NSW Independent Flood Inquiry](#), 21 June 2022.

Please do not hesitate to contact Sonja Hewison, Policy Lawyer on 02 99260219 or sonja.hewison@lawsociety.com.au if you would like to discuss this in more detail.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Brett McGrath', written in a cursive style.

pp.
Brett McGrath
President