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2 May 2023

Transitional Levy Consultation
Fire and Emergency New Zealand

Via email: TransitionalLevy2023@fireandemergency.nz

FMG'S SUBMISSION – TRANSITIONAL LEVY CONSULTATION

We welcome the opportunity to make a submission on the proposed increase to the Fire and Emergency New Zealand (*FENZ*) transitional levy.

In this letter, we provide our feedback on the proposed increase. We welcome the opportunity to discuss our submission in more detail if that would be of assistance.

Context - FMG

Farmers' Mutual Group (*FMG*) is the largest insurer of the rural sector in New Zealand holding 54% of the rural market. It is also a mutual - FMG's rural clients own FMG. Given that, FMG's purpose is to provide a better deal for rural New Zealand, with a vision to help build strong and prosperous rural communities. We achieve that by striving to provide our clients with competitively priced insurance products, quality risk-based advice, and through supporting numerous partners in the agricultural sector (commercial and charitable).

Profits are invested back into the business to support FMG's vision, purpose and ensuring a sustainable business. Consequently, FMG strives to generate profit, but *not* to maximise profits to ensure that our clients' premiums are affordable.

Impact for FMG's clients

Current environment likely to impact premiums

Despite FMG's goal of keeping premiums as affordable as possible for our clients, the current economic environment means that FMG's premiums will increase over the coming years. Those increases are driven by:

- inflation, which increases claims costs for insurers;
- changes to the Earthquake Commission Act cap and associated levy; and
- the increasing cost of reinsurance, which has been materially impacted by the Auckland Floods and Cyclone Gabrielle, in January and February 2023.

The proposed increase to the FENZ transitional levy is another cost which will ultimately be borne by insureds. For our clients, who are rural, the cost increases will be felt acutely. Inflation in the rural sector is significantly higher than the economy-wide rate of inflation and is currently tracking at 15 percent.

Increases to premiums, exacerbated by levy increases, will significantly increase the risk of policyholders making the decision to increase their levels of self-insurance. That of course has implications for FENZ's levy base (about which more below).

The levy increase is therefore extremely poorly timed.

Highlights limitations of current funding model
The increase to the transitional levy also highlights the risks and limitations of the current funding model.

We recognise that the basis of FENZ's funding is not within scope of this consultation. However, we feel it is important to touch on those risks and limitations now, given the context within which this levy increase has been proposed.

FENZ materially relies on New Zealanders to take out policies of insurance for its funding base. The higher the cost of insurance, the more incentive there is for policyholders to make the decision to either reduce their level of insurance, or not insure at all. As levels of self-insurance rise:

- FENZ' levy base erodes; and
- the "free-rider" problem inherent in the insurance levy funding model is exacerbated.

That is a real risk for FENZ in the current economic environment. That risk is *increased* by levy increases such as that proposed by FENZ.

Alternative funding models would, in principle, not be subject to those limitations. A non-levy-based model would also properly recognise the fact that FENZ's remit now extends beyond purely fighting fires, to resilience and readiness.

Impact for FMG
Aside from the obvious impact for our clients, FMG will need to invest material resource into updating our internal systems to ensure that we are in position to implement the levy increase by the "go live" date.

Assuming that the increase is limited to simple increases in the levy rate per $100 as suggested by the consultation document, FMG will require approximately 12 months to implement the changes. That is to allow adequate and robust testing of the system changes to take place.

If more complex changes are contemplated such as increases to the insured amount caps for levy purposes, or if there are any delays to the timings, then FMG may not be able to implement the required change by July 2024.

General
Thank you for considering this submission regarding the proposed levy increases. If you require any further information or have any questions, please contact me.

Yours sincerely,

Lisa Murray
Head of Compliance, Risk Quality, and General Counsel
FMG