30 April 2023

Transitional Levy Consultation
Fire and Emergency New Zealand
P O Box 2133
Wellington 6140

Email: TransitionalLevy2023@fireandemergency.nz

Submission on Fire Insurance Transitional Levy Increase Consultation

Please find attached the submissions of the Insurance Brokers Association of New Zealand Inc (IBANZ) to Fire and Emergency New Zealand.

Opening this public consultation on the eve of the Easter break leads respondents to believe the timing is a deliberate effort to restrict the period available for the wider consultations that are necessary, particularly in membership organisations.

The current economic environment, premium increases attributable to severe and more frequent weather events and the increased EQCover levy are putting pressure on the insurance decisions of households and businesses. Increasing the FENZ Levy will be the catalyst for some Insureds to reduce their insurance cover or simply stop buying insurance. Therefore, a longer consultation period would have been fair and reasonable.

IBANZ has over 100 member firms operating in the general (non-life) insurance market. IBANZ members employ approximately 5,000 staff of which approximately 2,500 staff are currently financial advisers.

IBANZ members place general insurance cover equating to approximately 50% of all general insurance premiums ($4.1 billion) for approximately one million New Zealand customers and for approximately 17 of the 20 general insurers operating in New Zealand. The total New Zealand gross written general insurance premiums in the 12 months to 30 September 2022 were more than $8.2 billion.[1]

Please let us know if you would like us to expand on any of the submissions made.

Yours sincerely,

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Melanie Gorham
CEO IBANZ Inc

[1] Insurance Council of New Zealand Market Data. Conservatively, an additional $424 million of cover was placed through Lloyds.

Submission form

Please use this form to make your submission on the proposal to increase the transitional levy on fire insurance contracts for the 2024/25 and 2025/26 years. **The closing date for submissions is Tuesday 2 May 2023.**

Submissions can be emailed to: **TransitionalLevy2023@fireandemergency.nz**

Alternatively, submissions can be posted to:

Transitional Levy Consultation
Fire and Emergency New Zealand
PO Box 2133
Wellington 6140

This submission was completed by:

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On behalf of (if an organisation)	Insurance Brokers Association of New Zealand Inc
Position (if an organisation)	General Manager

Please refer to page 8 of this discussion document for how we use your information, including considerations under the Official Information Act and Privacy Act.

☐ **Please tick here if you do NOT wish your personal information to be included in any summary of submissions that we may publish.**

Questions:

You do not need to respond to all our consultation questions. Feel free to limit your responses to those topics of most relevance or interest to you. **Please indicate any part of your submission that you believe should be withheld under the Official Information Act, and the reason(s) for withholding it.**

1. Do you agree that reducing costs for the years 2024/25 and 2025/26 would compromise Fire and Emergency's ability to provide services to communities and result in a failure to meet its commitments under the agreement with the NZPFU?

   No

   We are not convinced that reducing some operating costs would reduce the ability of FENZ to provide emergency services. Following are four issues that require further consideration to determine how cost effectively FENZ has managed more than $3.5 billion from levy payers since 2017.

No Financial Measurement of Efficiencies
It is not clear and has never been demonstrated that the costs of providing services is done so in an efficient and cost-effective manner.

The 2016 Cabinet Economic Growth and Infrastructure Committee paper forecast $47.7m for efficiency gains attributable to "improved use of capital, matching services with community risks and needs, and the use of a flexible service model ….". During the first four years after the merger it was planned that these savings be used to fund new support for volunteers and rural fire services. However, from 2021/2022 these efficiency gains could be used to offset the required revenue from levies. What evidence exists to show these efficiency gains were attempted and realised?

The 2017 Statement of Intent expressed 'efficiency and cost effectiveness' as being a feature of FENZ by 2021, however there is no evidence of this prudent financial practice before or after 2021.

The 2022-2023 Statement of Performance Expectations also expressed 'efficient and effective' measures, however; once again, there is no evidence or measurement of what those performance outcomes might be.

It appears there is a lack of any evidence to demonstrate the efficiencies resulting from the 2017 merger. To the contrary, there has only been increased cost.

No information is available to levy payers that the levy is being spent wisely although there is ample information compiled by the Taxpayers Union that suggests carefree spending is occurring rather than cost-effective spending (see the Taxpayers Union publication Cash to Ashes and their February 2020 press release about the FENZ rebranding costs).

Levy payers reasonably expect to know what cost efficiencies have been achieved because of the merger in 2017. For example, some of the spending has been rebranding of FENZ, the capital expenditure committed to stations in relatively small communities and the various communications and technology improvements.

FENZ has failed to demonstrate that the high level of services they aspire to achieve, are being delivered in a cost-effective manner.

Disproportionate Staff Increases
In the period since 2016, the Levy revenue to FENZ has increased by 62.7%, management and support staff have increased by 63.4% but the number of career firefighters has increased by just 1.8%. These figures alone suggest funding shortfalls should not occur and spending priorities are not given to the right areas.

The Regulatory Impact Statement relating to this proposed FENZ Levy increase comments that reducing operational costs such as staffing levels, frontline and back-office staff, has been considered (section 42) but was not seen as a viable option. However, the consideration of reducing staff is dismissed without transparency or objective justification, suggesting staff reductions have not been seriously or sincerely considered. Levy payers, whose funds are supposed to be protected through independent oversight by the Department of Internal Affairs, will assume that FENZ wants to increase the levy without any serious consideration to reduce operational costs.

FENZ Does Not Model 60% of Revenue
In the Regulatory Impact Statement, FENZ also acknowledge that "specific impacts within the non-residential policyholder group are also difficult to model because (of) the commercial sensitivity of insurance information".

Levies paid by non-residential policyholders represent approximately 60% of the total levy revenue. It is difficult to understand that FENZ cannot adequately analyse or model how such a large proportion of their revenue is generated or how the relevant policyholders might be affected by changes to the levy. Given this group of levy payers has an 'uncapped' exposure for the increase, they will be the most affected in terms of the amount of the increase compared to residential levy payers where the exposure is limited to the statutory levy cap. While the proportion of the levy paid by each levy group remains the same, we expect the impact on the non-residential policyholders will be greater and lead to increasing levels of underinsurance.

In terms of financial modelling, for many years FENZ has conducted audits and gathered data from insurers, brokers and direct levy payers under the transitional levy arrangement. Information available to FENZ includes the indemnity value(s) and levy calculation(s) that provide all the data necessary to adequately model levy rate changes. Levy payers should be extremely concerned about this weakness, within FENZ, when the new levy for July 2026 is considered.

Impact of NZPFU Settlement is Over-stated
FENZ attribute the NZPFU settlement as a substantial cause of the funding shortfall, contributing an additional $145m over the next three years. We might accept that the NZPFU settlement was justified however, this is just 7-8% of the levy revenue, more than $2 billion, anticipated over the same three-year period. What oversight exists for the balance of funds paid by insured businesses and households?

2. Do you agree with the proposal to increase the transitional levy for the 2024/25 and 2025/26 years to fund the increased costs outlined in this discussion document?

   No

   Please provide a brief outline of your reasons for agreeing or not agreeing:

   We disagree for the following reasons:

   1) Insurance is becoming less affordable. The current economic environment, premium increases attributable to severe and more frequent weather events and the increased EQCover levy are putting pressure on the insurance decisions of households and businesses. Feedback from our members (see our response to Question 10) already demonstrate that many Insureds are reducing their insurance cover or amount of cover, taking on more risk or simply not insuring. These circumstances will be exacerbated with any increase to the FENZ levy.
   2) An increased levy continues to illustrate the underlying inequity of the insurance-based levy model.
   3) The proposed 12.8% levy increase exceeds the current rate of inflation and we question whether this level of increase is justified, bearing in mind it is predicated based on the NZPFU settlement, or simply the consequence of FENZ having access to a revenue source where there is insufficient oversight.
   4) FENZ has stated that their revenue was unaffected by Covid. In fact, the revenue increased during a period when most organisations were negatively affected and FENZ continued developing their property portfolio, including using money from the Covid Response and Recovery Fund to support 26 rebuild and refurbishment projects (2022 -2023 Statement of Performance Expectations).
   5) Overall, we are not confident that $3.5 billion, collected as a levy between 2017 and 2022, has been spent in a cost-effective manner.

3. Do you agree that applying the increase as proposed is the simplest way to distribute the costs across different groups of levy payers?

   No

4. If you answered **No** to question 3, please provide details of any alternative you would recommend and why you recommend it:

   The simplest solution is to source the FENZ revenue through the same avenue as other government agencies – taxation. This solution is more equitable for all New Zealanders, more rapidly adaptable to the financial circumstances that FENZ has drawn itself into, and the robust oversight of Treasury.

   We also consider that given the change in the activities of FENZ to broader emergency response services, the government contribution of $10m does not adequately recognise the ‘public good’ component of the services provided by FENZ. We consider that a more meaningful contribution should be made and provided for as part of the annual budget.

5. Do you agree with the assumption that there will be growth in levy revenue of 2% per annum, to reflect inflation and increases to the number of policies, across all policyholder groups?

   No

   Households and businesses are actively controlling or reducing costs by reducing cover, reducing the amount insured or not insuring. This is evident from the feedback of our members and there is every likelihood the situation will deteriorate.

   The rate of business closures is increasing and the rate of new business registrations is reducing (Companies Office data for Q1 2023).

   In addition, through feedback from our members, we expect a high level of unpredictability over the next two years while households and businesses adjust to the economic environment. The likelihood is that cautious insurance decisions and a reducing number of operating businesses will offset any levy growth attributable to new businesses, new properties and increased indemnity values.

   Cost of insurance is increasing because of more severe and frequent weather claims, inflationary influence on all claims, operating costs, and reinsurance premiums of insurers. The higher EQCover levy is currently being added to premiums over the 12 months from October 2022. These issues do not affect the FENZ Levy however they do affect decisions made by residential insurance policyholders.

   Any FENZ Levy increase attributable to new business growth or new insured property or higher indemnity values is likely to be offset by decisions to buy less insurance or to not buy insurance at all.

6. Do you consider this growth projection a realistic assumption?

   No

7. If you answered **No** to question 6, please provide details of any alternative you would recommend and why you recommend it:

   Simply maintaining the insurance-based levy model and increasing the levy across all policyholder groups is **not equitable** and **delays** the alleged requirement for more funding.

   The most efficient and rapid solution is to source the FENZ revenue through the same avenue as other government agencies – taxation. This solution is truly equitable for all New Zealanders, more rapidly adaptable to the type of circumstances that FENZ is now facing, and the robust oversight of Treasury.

8. Are there other ways you think the levy could be increased to recover the additional costs?

   No

9. If you answered **Yes** to question 8, please provide details of your proposed alternative and the benefits and downsides of your suggested approach(es):

10. What impacts will the proposed increase to the transitional levy have on you? (For example, do you think it could impact your insurance costs or choices, spending on other goods and services, or non-financial impacts you think are relevant?)

To demonstrate the impact that an increase in the FENZ Levy will have on households and businesses we asked our members for their observations. This is what they wrote:

"Clients changed from replacement value to indemnity value especially partially occupied buildings; some small business owners cancelled their policy due to not enough profit." (Auckland)
"Avoiding valuations wherever possible. Considering First Loss, Indemnity Value and Functional Replacement basis. Also increased deductibles to save premium." (Wellington)
"Mainly higher excess options at this stage but we envisage more cancellations due to non-payment flowing through." (Auckland)
"Some are cancelling policies – particularly contents policies in the domestic space; taking higher excesses; some are reducing sums insured on plant and stock in the commercial space." (Auckland)
"More requests to drop cover or sum insureds due to cost pressure. We advise against this. We are seeing significant more uptake in voluntary excess." (Christchurch)
"Clients are asking for higher excess options to reduce costs, refusing inflation increases on covers and trying to reduce cover." (New Plymouth)
"Not so much in terms of under insurance but definitely have seem a spike in increased cancellations." (Upper Hutt)
"The increasing of this (FENZ Levy) in the market will certainly factor in the increasing insurance burden that people are voicing right now." (Invercargill)
"There has already been huge increases in the insurance market this year due to the increase in natural disaster events some of the premiums are increasing by 30-150% on it own plus the increase in EQC. Increasing the levy by 12.8% is going to increase the risk of people not insuring certain risks & underinsuring." (Invercargill)
"Reducing sums insured, removing coverage (for example BI), reduction in uptake of additional covers (i.e cyber), reducing motor cover to TPO; Reducing sums, dropping some covers." (Masterton)
"Not extending single period contract works insurance policies, not taking short term material damage cover when works complete and units haven't yet been sold, not commissioning new insurance valuations." (Takapuna)
"We are experiencing approximately 50% of our domestic customers wanting at least quotes for different options that can reduce premiums." (Takapuna)
"In the last month or so we are seeing a jump in clients looking to change cover mid-term, to reduce costs, and looking at cheaper policy options (particularly in domestic) to reduce pricing, but also this increases their exposure immensely." (Masterton)
"The discussion around pricing and how to reduce is happening in the vast majority of renewals." (Auckland)

11. Are there any other matters you consider relevant for implementing the proposed increase to the transitional levy.

Yes

12. If you answered **Yes** to question 11, please provide details of matters you consider relevant:

See comments under question 13.

13. If you are an insurer, how much time would you need to implement this change?

Our 100 member firms and their 5,000 staff are general insurance brokers. While not, insurers, our member firms are responsible to invoice their clients for the insurances they arrange, including the collection of any relevant FENZ levies. Therefore, they have business systems, which will need to be adjusted for any change to the FENZ Levy rate or its structure. There is a cost and lead-in time to implement any changes to be in a position to invoice changes to levies effective from 1 July 2024. Any time for implementation needs to take account not only of any system changes but also the lead in period for insurance renewals effective 1 July. The usual lead in period for renewals is three months prior to renewal. Therefore, a reasonable lead-in period for our members, allowing system changes and renewal processes, is six months.

Broker firm's operating systems can be both connected to and independent of an insurer's operating system. In most cases, the broker system cannot be adapted for changes until the associated change is implemented by the insurer.

Brokers need to make changes that are compatible with each insurer's system and their technical and documentation requirement, as well as for each of the affected policies and/or policy sections. As a result, the change of one FENZ Levy rate requires hundreds of adjustments to an operating system.

This type of project requires time-consuming engagement with technology personnel who will need to set aside other pre-scheduled projects that might have greater importance to the broker and their client.

For example, our members are already underway making system changes that are necessary to collate the unique information required by the regulator, Financial Markets Authority (FMA), as part of the Financial Advice Provider Regulatory Return. As a regulatory issue, this project must be given priority.

Another example: at least one of the broker networks has been developing a new operating system that is currently being implemented across their network. This project will deliver quality and efficiency benefits and it could be delayed while resources are temporarily re-directed for changes to the FENZ Levy, without compensation.

Suggesting that the insurance based levy model is simple, or the best option, or fit for purpose, ignores the considerable time and financial commitment of brokers and insurers to manage the levy (on an individual client basis) by determining exempt property, assess qualification of mixed-use properties, calculate the levy amount, obtain indemnity value declarations, conduct dialogue with levy payers, receive payment of the levy and on-pay the levy to insurers who, in turn, pay the levy to FENZ.

Typically, a client facing broker expends dozens of hours each year handling the levy assessment and its payment with their clients. Across our membership, we estimate that day-to-day FENZ Levy activity amounts to approximately $1,100,000 of broker time.