# fire**services** and the non-**insured**

## GREEN PAPER

Victoria
The Place To Be

Authorised by the Victorian Government
1 Treasury Place, Melbourne.

Printed by Stream Solutions
Level 3, 157 Spring Street, Melbourne, 3000



ISBN 978-1-921337-96-3

Published October 2009 by Department of Treasury and Finance
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Melbourne Victoria 3002
Australia

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Printed on recycled paper

# Treasurer's Foreword

The bushfires in February 2009 reminded all Victorians of the need to ensure our fire fighting services have the best equipment and best training available to respond to the annual threat of bushfires in our community.

Every Victorian understands the need to have well funded fire fighting services however there has been community debate following the fires on the best way to fund them equitably.

A review of the Fire Services Levy conducted by the Department of Treasury and Finance in 2003 found that, along with significant annual funding from the Victorian State Budget and Melbourne-based councils, the current model was the best way to fund Victoria's fire services. However, it is now appropriate to review the model again given that the Victorian Government has committed to reconsidering all aspects of our State's ability to prepare for and respond to major bushfires.

This Green Paper has been designed to help Victorians establish the best way to fund Victoria's fire services and to determine whether an alternative model would deliver adequate funding in a more equitable way.

I commend this Green Paper to you and look forward to your feedback.

**JOHN LENDERS MP**
**Treasurer of Victoria**

# GREEN PAPER – FIRE SERVICES AND THE NON-INSURED

## Why is the Government releasing a Green Paper?

The critical role of preventing and extinguishing fires on private property throughout Victoria is primarily the responsibility of two Government agencies: the Metropolitan Fire and Emergency Services Brigade (MFESB) and the Country Fire Authority (CFA). The Brumby Government wants to ensure these fire services continue to operate with sufficient resources, maintaining their vital role for all Victorians.

Currently, the annual budgets of the fire services are mainly funded through contributions that insurance companies are required to make, with the Government bolstering funding in the event of major fires to supplement suppression efforts. Insurance companies recover the cost of their contributions by attaching a Fire Services Levy (FSL) to insurance premiums.

This insurance-based funding model incorporates a risk factor resulting in high fire risk properties and assets contributing more to the funding of fire services than low risk properties and assets. For example a fish and chip shop pays a higher contribution than an accountant's office.

In 2003, the Victorian Department of Treasury and Finance released *A Review of Victorian Fire Services Funding Arrangements*. This report concluded that the current funding arrangement is stable, administratively efficient, cost-effective and ensures fire services have adequate funding.

Following the 2009 Victorian Bushfires (the Bushfires), several questions have been raised on the funding of the fire services through the current insurance-based model. The Bushfires have understandably led to a call on both Government and the insurers to pay for the increased ongoing cost from bolstering preventative and protective fire services. In particular, some suggest that the impost on the insured is too high and has become a disincentive for property owners to adequately insure. This is exacerbated by the fact that non-insured property owners who do not contribute towards the funding of the fire services receive the same protective fire services as insured property owners. The result is a funding burden spread across a smaller proportion of insured property owners.

Some of the properties that burnt during the Bushfires were not insured or were under-insured. The generosity of the donations to the Victorian Bushfire Appeal Fund appeal fund and the nature of the Government's financial support to those affected by the Bushfires may provide a disincentive for people to insure their properties in the future.

Unraveling these claims about insurance levels and funding implications is not easy, particularly as definitive evidence is not readily available or conclusive. Estimates of non-insurance vary from as little as 4 per cent to almost 30 per cent. This makes it difficult to assess whether criticisms of the current arrangements are significant and if there are alternative options to deliver fairer and sustainable funding of fire services.

It is therefore timely to undertake a study of fire services funding options, taking into account the full range of issues. As a result, the Victorian Government will examine the insurance-based model and the levels of under and non-insurance to determine the best model for fair and sustainable funding into the future.

This Green Paper is a draft policy document, designed to stimulate community discussion and invite public comment on the proposed policy response to the aforementioned issues. This feedback will be taken into account when working through policy options - including any further work arising from the 2009 Victorian Bushfires Royal Commission's (the Commission) final recommendations.

The Commission has not yet considered issues pertaining to insurance, but has indicated that it may broadly consider funding for fire services as well as the governance and administration of the MFESB and the CFA. This Green Paper will help the Commission consider these issues and will assist the Government in responding to the Commission's recommendations.

The first step is a proposed pilot study that will gather information to develop a greater understanding of the current levels of insurance throughout Victoria. The pilot study will also consider the effects the FSL has on insurance and assess options to improve equity in the funding of the fire services. Outlined in this Green Paper are a number of policy options for the funding of fire services.

While the Government supports the current funding model, the 2009 Victorian Bushfires exacerbated some of the criticisms of the insurance-based model. For this reason the pilot study will focus on option one as described in this Green Paper as the Government's current and preferred model.

After the Government considers feedback on this Green Paper, it will produce a White Paper, outlining its response and timetables for action. The White Paper will be released after the Henry Tax Review and the Commission's final report, to allow their findings to be considered in the paper.

# Background

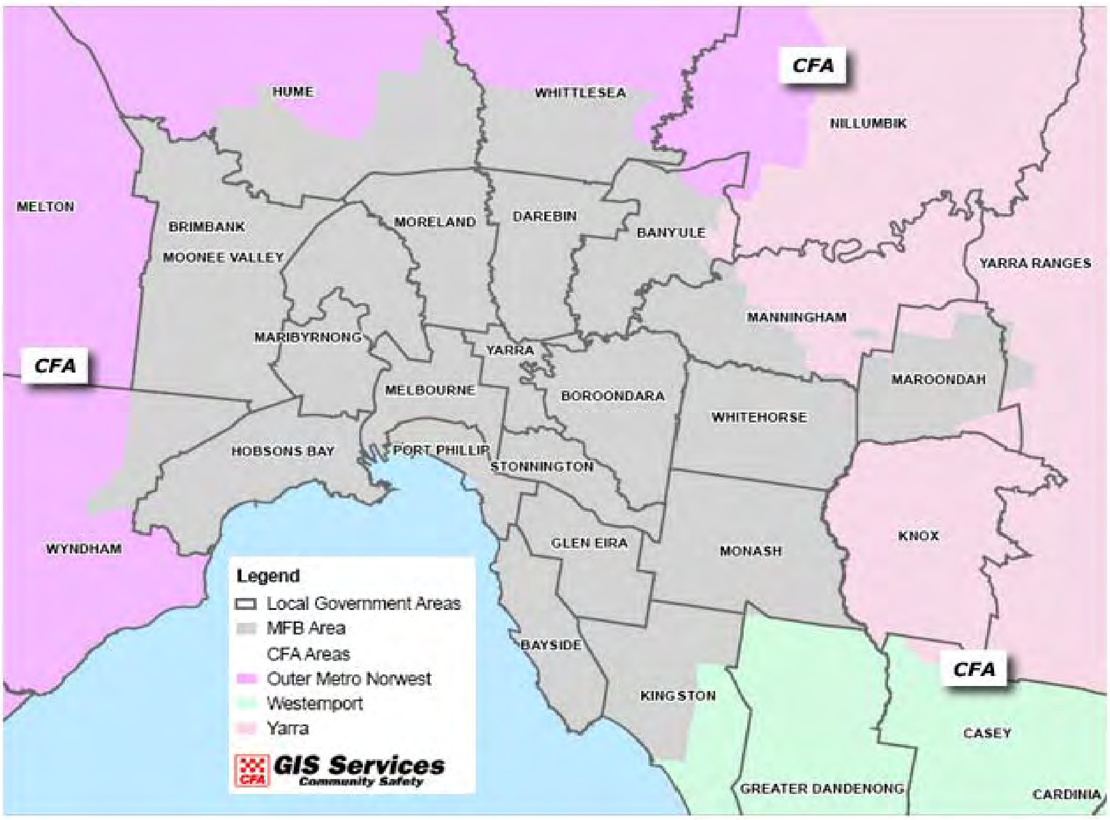
## *Operations of fire services*

The objectives of Victoria's two fire services, the MFESB and the CFA are to prevent, extinguish and contain fires.

The MFESB has 1 600 fire fighters who provide a 24-hour response to emergencies across the metropolitan fire district. They provide community protection, education services and emergency response from 47 strategically located fire stations and specialist departments.

The CFA has over 59 000 volunteers, supported by over 400 career fire fighters and officers, and more than 700 career support and administrative staff. The CFA covers an area of more than 150 182 square kilometres home to approximately 2.6 million people, which equates to roughly 50 per cent of Victoria's population. This area includes more than 980 000 homes, and covers all of rural and regional Victoria, including provincial cities and towns. The area also includes outer Melbourne suburbs such as Frankston and Dandenong, and key growth suburbs such as Cranbourne, Melton and Werribee as the map of the CFA and MFESB borders illustrates below.

**Chart 1: Map of the CFA and MFESB borders**




* Fire fighting and protection activities in State forests and National Parks are performed by the Department of Sustainability and Environment.

## *Beneficiaries of the fire services*

There are three main beneficiaries of fire services:

- Individuals or entities who could potentially suffer an injury or loss as a result of fire benefit, with property owners with a high fire risk and expensive property benefiting the most. Insurance policy holders also benefit from lower priced insurance premiums as insurance companies can lower the cost of their policies as a result of the reduced risk that fire presents due to fire services being available.

- Insurance companies benefit with payouts for property loss reduced, lessening the impact of fire losses on the companies' commercial returns. Fire risk is complex, and insurance companies, given their core business, are best placed to both determine and allocate this risk.

- The broader community benefits as fire services prevent the spread of fire to other properties and prevent further injury and loss.

This mixture of private and public benefit justifies a funding system based on a mixture of private and public funding.

In the MFESB area, evidence shows the commercial sector benefits more than the residential sector, while in the CFA area the benefits are roughly equal.

- In the residential sector, the share of benefits between buildings and contents are split roughly 3:1. Within the commercial sector, there is a wide variation in the benefits received because assets, including buildings, pose different levels of risk depending on a range of factors (such as materials used in building construction and the type of business undertaken).

- Motor vehicle owners receive around 15 per cent of benefits.

## *Funding of the fire services in Victoria*

The MFESB and CFA are funded by the insurance industry contribution, local government and the State Government through statutory contributions. The proportion of funding by the different sectors, as detailed in Table 1, is determined under Section 77A of the *Country Fire Authority Act 1958* (CFA Act) and Section 37 of the *Metropolitan Fire Brigades Act 1958* (MFB Act). Insurance companies are required to contribute 75 per cent of the MFESB annual estimated expenditure and 77.5 per cent of the CFA annual estimated expenditure. The actual funding levels for 2009-10 are detailed in Table 2 below, which also demonstrates that the State Government's contribution to the CFA is two and a half times higher than its contribution to the MFESB in dollar terms.

**Table 1: Fire services statutory funding sources**

| | MFESB | CFA |
|---|---|---|
| **Funding Source** | **Statutory Contributions (%)** | **Statutory Contributions (%)** |
| **Insurance companies contributions** | 75.00 | 77.50 |
| **Local Government** | 12.50 | - |
| **State Government** | 12.50 | 22.50 |

Insurance companies have been involved in the funding of the fire brigades in Victoria since their inception in 1845. The current system of funding the fire brigades through statutory contributions from insurance companies has remained relatively unchanged over the last 20 years.

**Table 2: Annual budgeted funding of fire services: 2009-10**

| | MFESB | | | CFA | | |
|---|---|---|---|---|---|---|
| **Funding Source** | **$** | **All Sources (%)** | **Statutory Contributions (%)** | **$** | **All Sources (%)** | **Statutory Contributions (%)** |
| **Insurance companies contributions** | 206 133 060 | 66.85 | 75.00 | 303 169 287 | 75.30 | 77.50 |
| **Local Government** | 34 355 510 | 11.14 | 12.50 | - | - | - |
| **State Government** | 34 355 510 | 11.14 | 12.50 | 88 016 890 | 21.86 | 22.50 |
| **Other Revenue (forecast)** | 33 507 000 | 10.87 | - | 11 412 000 | 2.83 | - |
| **Total** | **308 351 080** | **100.00** | **100.00** | **402 598 177** | **100.00** | **100.00** |

**Notes:** Statutory insurance companies, local government and State contributions: amounts approved by Governor-in-Council. Other revenue: estimates only, includes interest, sales of goods and services (e.g. provision of services), other revenue (e.g., fines).

Insurance companies identify their contribution costs to policy holders as FSL on insurance premiums. The Insurance Council of Australia (ICA) provides their members with quarterly advisory rates to add to premiums. Insurance companies are not obliged to recover the costs in this way.

There are provisions under the CFA Act (section 87(2)) and MFB Act (Section 44) to directly charge non-insured property owners for services. The CFA and MFESB have a policy where they seek to impose charges fairly. In principle, the fire services will impose charges unless there is an acceptable reason to waive it, for example, if the damage to the property is less than $1 000 or the owner/occupier is receiving Centrelink payments.

These provisions allow the fire brigades to recover the costs of their services from the non-insured in the event of a call out. However, in practice, fire services recover costs mostly from businesses rather than individuals. This may lead to insured people providing a disproportionate amount of fire services funding.

## *Funding of Fire suppression and prevention activity*

The Government's statutory contribution to the annual budget of the CFA and MFSEB should be not looked at in isolation to the total costs of funding fire prevention and suppression activities. The most recent fire season demonstrates the magnitude of the total fire effort in Victoria (refer Table 3).

According to the latest Productivity Commission's *Report on Government Services (ROGS)*, Victoria's expenditure per person on fire services has increased from the second lowest in 1999, when the Labor Government was elected, to currently being the highest in the country, recognising that Victoria is a fire prone State.

In 2008-09 more than $186 million was spent by the Department of Sustainability and Environment (DSE) on suppression and prevention activity, including DSE fire fighting on public land and controlled fuel reduction burning.

The State Government makes a significant statutory commitment to the annual CFA and MFESB budgets. When added to the total annual funding of other Government agencies such as the Office of the Essential Service Commissioner and the State Emergency Service budgets, the Emergency Management Capability funding totals $200 million.

In the event of a major fire, the State Government meets the cost over and above the amounts budgeted for fire suppression activity. The 2008-09 bushfire season illustrated this, with the Government paying almost $600 million in supplementary funding towards the fire suppression effort. This funding goes towards suppression efforts including additional aircraft appliances and flying time for services provided by the likes of the well known *Elvis* air-crane, funding for project fire fighters, construction of fuel breaks and containment lines, and costs associated with services provided by international and interstate fire fighters.

The figures below do not include the contribution by the Brumby Government to the bushfire recovery and reconstruction effort.

**Table 3: The 2008-09 fire suppression effort**

| | 2008-09 $m |
|---|---|
| Total State Government Contribution | 979.7 |
| • *Land and Fire Management Output (DSE funding)* | *186.5* |
| • *Emergency Management Capability Output funding (DoJ funding, e.g. CFA, MFB, OESC, VicSES)* | *200.0* |
| • *Supplementary Budget Funding (Treasurers Advance)* | *593.2* |
| Insurance Contribution (CFA and MFESB) | 426.8 |
| Local Government Contribution (MFESB) | 32.9 |
| **Total Fire Prevention and Suppression Effort** | **1439.4** |

Department of Sustainability and Environment (DSE), Department of Justice (DoJ), Office of the Essential Services Commission (OESC), Victorian State Emergency Services (VicSES)

## *Funding mechanisms in other states*

The funding of the fire services varies between the states in Australia and New Zealand, from insurance-based models (such as Victoria's), to property-based models and hybrid models that are a mix of property and insurance-based models.

New South Wales has a similar insurance-based funding system to Victoria. The State has a metropolitan based service, NSW Fire Brigade (NSWFB) and regional fire service (RFS), with funding provided by insurance companies, local government and the State Government. The proportions paid by each are identified in table 4:

**Table 4: NSW funding of fire services**

| Funding Source | NSWFB (%) | RFS (%) |
|---|---|---|
| **Insurance companies** | 73.7 | 73.7 |
| **Local Government** | 12.3 | 13.3 |
| **State Government** | 14.0 | 13.0 |

New Zealand also has an insurance-based funding model to fund their fire services. It is also worth noting that New Zealand has a natural disaster statutory insurance scheme that is administered by the New Zealand Earthquake Commission. The scheme provides insurance for natural disasters to residential property owners against damage caused by earthquake, natural landslip, volcanic eruption, hydrothermal activity or tsunami; in the case of residential land, a storm or flood; or fire caused by any of these. Dwellings are insured up to a maximum of $100 000 and personal effects are insured up to $20 000. The scheme is funded through a compulsory charge added to home and contents insurance premiums, which is passed onto the Earthquake Commission.

Tasmania recovers costs from local government through property rates and from insurance companies through premiums, that is, a hybrid system.

Western Australia has a property-based funding system where an Emergency Services Levy is imposed on the gross rental value of immobile property. The Western Australian Government provides further funding to pay for benefits given to fire and emergency service volunteers.

South Australia also imposes an Emergency Services Levy on the improved value of motor vehicles and on immobile property.

In Queensland, the fire and rescue services are funded by a property-based Urban Fire Levy (73 per cent), the Queensland Government (10 per cent), other State Government funding sources (9.6 per cent), and user charges (5 per cent).

## Gap analysis of the current system

### *Equity and efficiency*

The current insurance based model is efficient and equitable, providing a stable and administratively efficient source of funding to the fire services. As the FSL is charged as a proportion of insurance premiums, the contribution of individuals to the fire services is linked to fire risk and asset value. People who have more valuable assets in high fire risk areas contribute more to funding fire services than those with low value assets or low fire risk. This is not necessarily the case in property-based funding models. The insurance-based system also encourages fire risk management, as insurance companies will potentially offer lower premiums to those individuals who have taken steps to reduce fire risk on their properties.

However, the current arrangements allow those who are not insured or who are under-insured to benefit from the provision of fire services without directly contributing to their funding. As noted earlier, the fire services do not often recover costs from non-insured residential properties despite having the power to do so.

This inequity in the system, where non-insured property owners do not contribute to the fire services is particularly noticeable in light of the 2009 Victorian Bushfires. It would be inappropriate for the CFA to begin issuing notices for call out charges to non-insured properties razed by the catastrophic 2009 Bushfires. Nonetheless, millions of dollars worth of fire services were provided during the 2008-09 fire season to such properties. Whether inequity exists in the current arrangements can only be determined by assessing whether those who are facing comparable fire risks are paying similar contributions to the cost of fire services.

The decision by an individual or company not to insure a property and therefore not contribute to the funding of the fire services may not be inequitable in itself. For example, a person may have chosen not to insure because they reside in a low fire risk area. Similarly, many large commercial businesses self-insure and then pay the cost of the fire services they have received when charged by the CFA and MSEFB.

There may be some cases where the affordability of insurance is an issue. It may be appropriate for low income pensioners to be charged at a concessional rate. How these concessions are determined and paid for would need to be considered in the design of options. For example, community service obligation payments[1] from the Government's budget may be considered to fund any concession.

The fact remains that there is a proportion of property owners who are not insured and therefore do not contribute to fire services but are afforded the same access to them as those with insurance.

## *Analysis and evidence of non-insurance*

Currently, the best available informative data on the levels of under-insurance and non-insurance is drawn from reports and data analysis conducted by the ICA and the House Expenditure Survey (HES) conducted by the Australian Bureau of Statistics. The experience of the 2009 Victorian Bushfires have also provided information in this area. This information is summarised below, however much of the available information is inconclusive or contrasting. Further research and analysis is required to determine whether the non-insurance is actually a significant issue.

## *Insurance Council of Australia - The non-insured: Who, why and trends*

The ICA report, *The non-insured: Who, why and trends* released in May 2007, draws from a Roy Morgan Single Source Survey and data from the 2003-04 Australian Bureau of Statistics HES to conduct an analysis into the rates of non-insurance and the profiles of non-insured property owners. The HES survey found that 23 per cent or 1.8 million households had no expenditure on building and contents insurance.

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[1] Community service obligation payments are payments for which the cost of a subsidy is explicitly identified by the Government and then paid for directly by the Government. For example, under the transport accident scheme, pensioners are subsidised around 50 per cent of the cost of their premium (i.e. they pay half what they would pay if risk alone was taken into account) – the balance is then paid by Government or is cross subsidised by the other policy holders in the scheme.

There is evidence that the level of non-insurance in Victoria is similar to other states and close to the national average. Data does not show any significant differences between states with insurance-based funding models (Victoria, NSW) and those with property-based funding models (WA, SA). Table 5 below summarises the data.

**Table 5: Average non-insurance rates (5 years to 2007)**

| | No building insurance (%) | No contents insurance (%) | No building or contents insurance (%) |
|---|---|---|---|
| **VIC** | 10.5 | 14.1 | 8.8 |
| **NSW** | 11.9 | 17.3 | 10.5 |
| **QLD** | 8.8 | 12.1 | 7.0 |
| **WA** | 10.1 | 15.1 | 8.8 |
| **SA** | 6.5 | 9.0 | 5.2 |
| **TAS** | 6.2 | 8.0 | 4.8 |
| **ACT** | 7.7 | 13.1 | 6.0 |
| **NT** | 8.1 | 17.4 | 5.6 |
| **National Average** | **10.1** | **14.3** | **8.6** |

Source: Roy Morgan Single Source Survey over 5 years to 2007, provided by the Insurance Council of Australia.

## *2009 Victorian Bushfires*

The Department of Human Services has reported to the Victorian Bushfire Reconstruction and Recovery Authority (VBRRA), that due to the 2009 Victorian Bushfires:

- 2 131 properties were destroyed; and,
- 1 389 of the properties destroyed were primary residences.

As of 30 July 2009, the ICA reported that following the Bushfires, there were 1 853 'total loss' insured properties (requiring reconstruction or significant repair before reoccupation).

These figures suggest that approximately 13 per cent of total loss residential properties may not have been insured in bushfire affected areas. It should be noted that the ICA has suggested that these estimates do not capture the level of under-insurance that was prevalent in fire affected areas. The ICA also believes that non-insurance rates in the bushfire affected areas are higher than in other parts of Victoria due to the demographics, i.e. lower income rural households are more likely to be non-insured.

The different definitions of a 'total loss' by VBRRA and the ICA make it difficult to draw definitive conclusions about the level of non-insurance rates in the bushfire affected areas. However, the data above relating to the 2009 Victorian Bushfires does indicate that there is a significant level of non-insurance.

### *Why don't people insure?*

There is no evidence that suggests people are not aware of the risks to their home and contents. Insurance is a product that is generally available and affordable to cover these risks. So then, why don't people insure?

The previously mentioned ICA report *Non-insured: Who, why and trends* examines the profiles of non-insured property owners and the effect of government policies on insurance levels.

In the report, the ICA asserted that:

- Home type and tenure are important factors affecting insurance levels for both building and contents cover, although demand for contents insurance appears to be more price sensitive than building insurance.
- Non-insurance is lower for those with a mortgage, although non-insurance escalates the longer the homeowner has had a mortgage.
- Individuals with fewer savings (and therefore more vulnerable to loss) are more likely to be non-insured.
- Non-insurance is more prevalent at the early stages of life (e.g. singles, the young).
- Non-insurance is more prevalent in urban centres and in particular, specific urban localities in the major capitals.
- State taxes impact on insurance levels - states with high levels of insurance taxes have higher rates of non-insurance. However, as noted above, there is no evidence to suggest that non-insurance is higher in states with insurance-based funding models as compared to states with property-based funding models.
- A certain level of non-insurance will always exist. There are many reasons for this, including age, income and education levels. It cannot be expected that 100 per cent of the population will always have home or contents insurance.

## Pilot study

To help determine the viability of the different options presented in this paper, analysis is required to develop a reliable estimate of the levels of non-insurance and under-insurance. There are a currently range of estimates making it difficult to assess whether it is a significant issue and whether the options presented correctly address the problem.

The pilot study will collect data for several municipalities to determine the levels of non-insurance and under-insurance. From this information, a cost benefit analysis of the options can be undertaken. The State Revenue Office (SRO) and Department of Treasury and Finance (DTF) will conduct the pilot study.

The ICA or insurers will be asked to supply information about properties they have insured in the sample geographic regions. The SRO will cross-check this with information they have about properties and property values. Based on this cross-matching:

- a more reliable estimate of the degree of non-insurance and under-insurance will be determined; and
- this information will be used to assess the feasibility of various policy options being considered in this paper.

For the options that are feasible, the study will assist in the development of any key design and implementation features such as what levy rate to charge under option one or, how to define under-insurance.

The study will also look at whether it is possible to use Capital Improved Value (CIV) as a benchmark against which to assess under-insurance. All municipalities collect information on CIV, which is provided to the SRO. This could be used as a starting point for valuing a property for insurance purposes, recognising that CIV does not necessarily match the value of the building structures. Adjustments would need to be made to such data. For example, the component of CIV that relates to the value of the underlying land would need to be removed.

In order to understand the depth of the issue and run the pilot study, new state legislation will need to be enacted or existing legislation amended to address privacy issues so that the Government can obtain data from insurance companies.

When providing this information, insurers would be obliged to comply with the National Privacy Principles (NPP) in the Commonwealth's *Privacy Act 1998* (Privacy Act) regarding the collection, use and disclosure of personal information.

It may be necessary for insurance providers covered by the *Privacy Act* to change their Product Disclosure Statements or other relevant policies to meet their prospective NPP obligations. Some insurers may need to make this change to contribute to the pilot study. Insurers may also need to make such a change at a later stage should the Government's White Paper response involve a change to the current arrangements.

## Options to address the fairness of fire services funding

The Government's key policy objective in relation to fire services is to improve the equity in the distribution of fire services costs. Factors to be taken into account when assessing alternative options include:

- ***Efficiency and equity*** – those who benefit from fire services are funding the costs of its provision. There is a close alignment of funding contributions and benefits that encourage those generating fire risks to recognise and manage them.

- ***Transparency and simplicity*** – it is clear and easy for the community to understand what they are contributing funding for and how much they are contributing.

- ***Revenue stability*** – funding needs to be sufficient to meet the expected service costs.

- ***Administration and compliance costs*** – Government administration and private sector compliance costs are an acceptable proportion of the funding collected to support fire services.

- ***Transitional costs*** – the cost of implementing any option does not reduce the funds available for supporting fire services.

Based on a preliminary assessment against these factors, the Government's preferred option is the existing approach (option one). However, the Government is interested in seeking the public's comments and views on the current model and the alternatives.

## Examining the options

### *Option one: Retain the existing approach*

For those insured, the current insurance-based funding model is that the FSL reflects asset value and risk, including fire risk. Insurance companies provide expert actuarial advice on the fire risk of individual policies on different types of properties.

An insurance-based fire services funding model incorporates a risk factor in the sharing of the fire services costs. This means that policy holders with high fire risk properties and assets contribute more to the funding of fire services than those with low fire risk properties and assets. For example, a fish and chip shop and an accountant's office would pay different rates based on risk.

Under a property-based system, fire risk is no longer a determinant of funding contributions, and therefore funding contributions are redistributed away from property owners who generate the greatest fire risk. The incentive to better manage high risk properties is also weakened. Most low risk properties that are fully insured are likely to pay significantly more under a uniform rate property levy. Also, as the levy is only linked to property values, the funding burden within the residential sector falls fully onto building owners, with contents owners making no direct contribution. Moving to a property-based system would also add another administrative cost to collecting the contributions.

The evidence provided to date does not indicate significant differences in insurance levels between jurisdictions with property-based models and Victoria which currently has an insurance-based model.

Questions for consideration:

- Is the lack of parity in fire services funding created by the level of non-insurance and under-insurance significant enough to warrant a change to the current arrangements?
- Does the increased fire effort put too much strain on insurers who along with Government are having to meet this cost?

## *Option two: Charging a levy on non-insured and under-insured property owners*

Property owners who do not insure or adequately insure their properties above a statutory amount would be charged a levy which would have the dual purpose of providing an incentive for people to insure their properties and spreading the burden of fire services funding. This would ensure that those who choose not to insure are still making a contribution to the costs of the fire services.

This option builds on a number of the features of the current arrangement, in particular, the insurance-based framework.

The intended outcomes of this option are:

- a broader pool of contributors to the target of Victoria being fire ready; and
- improved take up of insurance which has benefits to the State above and beyond the question of funding the fire services.

Both of these outcomes would reduce the average cost of insurance, with the second outcome doing so to a greater extent as it spreads both insurance risk and the FSL burden.

A levy could be designed with the following characteristics:

- a percentage of property value (to take into account the asset value);
- separate commercial and residential rates and/or metropolitan and rural rates;
- split into different risk ratings (e.g. properties in high fire risk areas, pay higher rates); and
- set at a rate to encourage the take-up of insurance.

The design of a levy would also need to take into account two issues:

- the definition of 'under-insurance', with a legislative benchmark potentially required such as set percentage of the CIV of a property; and
- the determining factors of deciding not to insure, such as affordability and financial literacy.

| Questions for consideration: |
| --- |
| • Is the option outlined above an appropriate way to target non-insured and under-insured property owners, to ensure their contribution corresponds with the level of benefit they receive? |
| • The factors that influence insurance take-up involve a number of socio-economic triggers. Are there any social policy issues that would need to be considered if implementing this proposal? For example, should there be concessions through exemptions or subsidies for low income groups and how could these be funded? |

### *Option three: Status quo plus mandating banks to issue compulsory insurance*

Banks would be asked to state that property owners must establish and maintain property insurance as a condition of their mortgage. Banks would check this annually to ensure compliance. Currently, most banks require mortgage holders to insure their property for the first year of the mortgage only.

This option would result in an administrative cost to banks as it would involve compliance checks and auditing. However, it is already in the interest of the banks for mortgage holders to have property insurance throughout the course of their loan.

It is difficult to gauge how many property owners with a mortgage do not have property insurance. However, it is likely that most people with a mortgage have insurance. This option does not address non-insurance or under-insurance by property owners who do not have a mortgage. Around 65% of Victorian households did not have a mortgage in 2006 according to the Australian Bureau of Statistics.

The constitutional responsibility for regulating banks rests with the Commonwealth Government. The Victorian Government would need to address this issue with the Commonwealth Government as otherwise it could only 'encourage' banks to improve their practices voluntarily.

Question for consideration:

- How would this option address the question of equity outside of properties that are mortgaged?

## *Option four: Introduce compulsory fire services insurance*

Every property owner would have to take out “fire services” insurance. The Victorian Government could mandate that fire services insurance is compulsory and could be offered by insurance companies.

This would be similar in concept to the Compulsory Third Party (CTP) personal injury insurance schemes in New South Wales, Queensland and Victoria.

The policy reasoning behind CTP personal injury insurance, such as the Transport Accident Commission scheme in Victoria, is that third parties can be injured in a transport accident. However, governments do not compel individuals to purchase private property insurance for their motor vehicles under any of the existing CTP schemes. A similar argument could be made for the fire services. There is a public benefit in the containment of fires to a single individual’s property (rather than spreading to other properties– effectively third parties), but not to cover the cost of damage to the individual’s actual private property.

The Government would be required to monitor and audit compliance under this option. As with options two and three, this would require insurance companies to provide data so penalties could be imposed on policy holders that do not comply.

Questions for consideration:

- Is this option an appropriate way to target non-insured and under-insured property owners to ensure their contribution to fire services corresponds with the level of benefit they receive?
- Does the compulsory nature of this proposal raise Charter of Human Rights concerns?
- The factors that influence insurance take-up involve a number of socio-economic triggers. Are there any social policy issues that would need to be considered when implementing this proposal? For example, should there be concessions by way of exemptions or subsidies for low income groups and how could these be funded?
- Does this option discriminate between fires and other natural disasters (e.g. flood)? Should the levy be applied to cover all natural disasters, e.g. an emergency services levy as opposed to a fire services levy?

### *Option five: Introduce compulsory property insurance*

All property owners would have to take out property insurance offered by private insurance companies and the current FSL approach would be maintained.

This option would reduce the level of non-insurance, ensuring that the burden of funding fire services is spread across more property owners.

Over time, insurance may become unaffordable in fire prone areas for some individuals or businesses. Compulsion would increase the volume of homes covered, spreading the cost of premiums across a greater number of homes (and better reflecting the risk). However, some property owners choose not to insure their properties for reasons other than low income. This option would remove this choice.

Enforcing this option may be difficult. The Government could make insurance a requirement of building approval in the same way as domestic building insurance. The Government could also make it a requirement of sale/transfer for existing properties. However, this would not capture homes that are not sold, and may be seen as an impediment to the property market.

An added complication is that it would be difficult for the Government to ensure the insurance level obtained is at a level appropriate for the value of property. The Government could address this by producing a value and risk index map of Victoria. This would zone the State into various areas as a guide to the level of risk in each area. This would require a consistently applied definition of what is a fire prone area, with data being available to support this definition. This may be difficult to obtain without data from insurers.

The Government would be required to monitor and audit compliance under this option. Like options two and three, this would require insurance companies to provide data so that penalties can be imposed on policy holders that do not comply.

Questions for consideration:

- Is the option outlined above an appropriate way to target non-insured and under-insured property owners, to ensure their contribution to fire services corresponds with the level of benefit they receive?
- Does the compulsory nature of this proposal raise Charter of Human Rights concerns?
- The factors that influence insurance take-up involve a number of socio-economic triggers. Are there any social policy issues that would need to be considered when implementing this proposal? For example, should there be concessions by way of exemptions or subsidies for low income groups and how could these be funded?

## *Option six: Replace the FSL with an 'across the board' property tax (which could be risk based)*

A levy would be imposed on property values to replace insurance companies' statutory contributions. The rates would be set at appropriate levels for the residential and commercial sectors and for regions based on risk. This would maintain the current FSL collection shares.

The risk-based approach could be high level (sector, region specific) or could attempt to map risks to a finer level of detail.

Removing the FSL from insurance premiums could potentially deflate insurance premium costs and could encourage some people to take up insurance. This option would also result in every property owner contributing to the funding of the fire services.

However, it may be difficult for the Government to ensure the levy is collected and is set at a level appropriate for the value of property.

This option would also mean that the SRO would need to issue a new tax assessment to every one of the property owners of the 3 million parcels of land in Victoria annually.

Questions for consideration:

- Is the option outlined above an appropriate way to target non-insured and under-insured property owners to ensure their contribution corresponds with the level of benefit they receive?
- Does the compulsory nature of this proposal raise Charter of Human Rights concerns?
- Does this model reduce the incentive to manage fire risk?
- How can the Government continue to charge insurance companies for the benefit that they derive from the provision of fire services?
- What transitional issues are likely in a major change in funding models to establish a new collection system?

## *Option seven: Require mandatory collection of costs from non-insured by the CFA and MFESB*

This option would remove the MFESB and CFA discretion to waive costs in the event of a call-out to a non-insured property.

The proposal would encourage more people to take up insurance. It would also resolve the issue of non-insured individuals or companies benefiting from the fire services but not contributing to the cost of fire services.

The proposal is likely to be more effective in encouraging the take up of insurance as the cost of individual call-outs would be expected to be significantly higher than a property levy (where costs would be spread across all property owners).

Any assessment of this model would need to consider affordability for low income groups and financial literacy, and the appropriateness in circumstances such as Black Saturday of billing displaced and distressed property owners after a fire.

Questions for consideration:

- Is the option outlined above an appropriate way to target non-insured and under-insured property owners to ensure their contribution corresponds with the level of benefit they receive?
- Would this proposal adequately address the issue of under-insurance?
- The factors that influence insurance take-up involve a number of socio-economic triggers. Are there any social policy issues that would need to be considered when implementing this proposal? For example, should there be concessions by way of exemptions or subsidies for low income groups and how could these be funded?

Question for consideration across all the options:

- Would the administrative burden under a range of options be manageable from a regulatory burden perspective?

# Have your say

The Government wants to give all Victorians the opportunity to comment on the ideas put forward in this green paper and to convey their views on how Victoria can equitably fund our Fire Services.

Generally, all submissions would be treated as public documents unless individuals or organisations request otherwise. Please note that freedom of information access requirements will apply to all submissions including those treated as confidential.

Submissions will be called for from June 2010 with a closing date for comment on the green paper of 15 July 2010. Submissions can be sent:

## *By post:*

Fire Services Project
Department of Treasury and Finance
1 Treasury Place
East Melbourne
Vic 3002

## *By email:*

**fireservicesproject@dtf.vic.gov.au**

## Timing/Next Steps

**STEPS TO THE FIRE SERVICES FUNDING WHITE PAPER**

| | |
|---|---|
| **Step 1**<br>***October 2009*** | The Green Paper is announced and released for wider community consultation, which:<br>- presents a range of options to be assessed to determine if the best arrangements are in place to ensure sustainable funding of fire services and that funding of those services is as fair as possible; and<br>- outlines a pilot study that will collect and analyse data for this purpose. |
| **Step 2**<br>***November 2009 to December 2009*** | Legislation is introduced and passed to enable the pilot study to be undertaken. |
| **Step 3**<br>***December 2009*** | The Commonwealth Henry Taxation Review presents its final findings to the Commonwealth Government. |
| **Step 4**<br>***January 2010 to June 2010*** | The SRO and DTF compile information from insurers, and undertake analysis and modeling of the options presented in the Green Paper, taking into account the submissions that have been provided from the community. |
| **Step 5**<br>***June 2010 to July 2010*** | The Government receives written submissions in response to the questions that are canvassed in the Green Paper. Submissions on the Green Paper are to be provided by 15 July 2010 to:<br>Fire Services Funding Review<br>C/- Department of Treasury and Finance<br>1 Treasury Place<br>East Melbourne 3002<br><br>email to: fireservicesproject@dtf.vic.gov.au |
| **Step 6**<br>***End-July 2010*** | The 2009 Victorian Bushfires Royal Commission releases its final report on 31 July 2010. |
| **Step 7**<br>***August 2010 to February 2011*** | The Government considers all feedback, comments, ideas and suggestions, the findings of the Henry Tax Review and the Royal Commission final report, as part of its formulation of a final position for the White Paper. The White Paper will be released within six months of the Royal Commission handing down its final report. |