

ADDRESS TO AICC IN DEFENCE OF THE INSURANCE INDUSTRY

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INTRODUCTION

Thank you all for coming today and thank you to the Chamber for inviting me to speak.

Three things are going to happen today.

First, you are going to enjoy lunch and meet some interesting people from other organisations, reason enough for coming along.

Second, I am going to use my many years of experience in the insurance industry to promote its role as a vital part of Australia's fabric and an economic shock absorber in times of natural disaster. And finally, you are all going to walk out of here this afternoon and advocate on behalf of the industry next time you hear someone take a pot shot at insurers. Failing that, as they say two out of three ain't bad.

THE BIRTH OF AN INDUSTRY

Insurance has been around in some guise for thousands of years.

Over the centuries, people have joined together and cooperated to reduce risks and preserve wealth.

At its most primitive people lived in groups to reduce the risk of attacks from wild animals and to increase the amount of food that could be gathered or hunted.

In about 5,000 BC, instead of putting all their property in just one boat, Chinese traders spread their goods over several boats. If one boat sank, no individual trader went broke.

Sharing the risk was an early form of insurance and today that principle equally applies – we collect premiums from many to pay the insurance claims of a few, preserving wealth across all the community.

ROLE OF INSURANCE

Before looking at some of the commentary made about the industry of recent times I would like to take a moment to outline what insurance really means for each of you in the room today.

For many of you who haven't had to make a claim, insurance is just a bill or transaction at best, or a resented grudge purchase at worse. Indeed, many think that if they go a year without making a claim they get no value from having an insurance product.

Our head office here in Sydney is adjacent to the Apple store, and while I don't ever expect people will be camping in front of one of our branches to buy our latest product like I see them do across the road, the two are connected.

Insurance gives individuals the freedom to live their lives every day in the knowledge that they have protection that supports their lifestyle. They can protect their new Apple I phone, I pad or whatever it was that got them so passionate that sleeping on the pavement seemed like a good idea.

The fact is, insurance provides value every day, and you use it every day – claim or no claim. Every time you get in your car or open your front door you know that your asset has been protected and that you can be put back to where you are now should the worst happen. It gives you confidence and improves quality of life. There is value in that every day.

At a more macro level the industry supports our economy and protects the taxpayer.

First, it pays more than \$80 million dollars in claims each and every day. \$80 million. That removes the burden on the government and individuals who would otherwise have to support the loss. It frees up funds to be used in more productive ways. When people drop out of insurance it is ultimately the taxpayer who foots the bill when disaster strikes.

Second, the industry underpins nation building – economic activity is possible because insurance protects the industries and individuals in all pursuits, whether that be building a national highway or giving professional advice in business and private practice.

It's also worth noting the financial services industry is an employer and generator of wealth. The financial and insurance services industry employs almost 400,000 people and its recent growth rate of 3.3% has been

concentrated largely in the insurance and superannuation sectors. IAG alone employs around 13,000 people – the majority here in Australia.

It is an industry I am very proud to be involved in and I'm proud of the efforts of everyone who has supported insurance customers not just in this challenging period, but for the more than one hundred and eighty years that I can trace the industry's physical presence in this country.

WHERE WE'VE BEEN

The number of natural disasters we have had in recent times won't be a surprise to anyone here today.

You only have had to turn on a television or open a newspaper to be confronted with images of loss, destruction, and in the most tragic of circumstances, death.

Let me give you a sense of scale to some of those pictures you've seen.

2011 was the worst year on record for natural disasters in this country. Insured losses from catastrophes were around \$5 billion.

Cyclone Yasi, more than 72,000 claims representing around \$1.3 billion, Queensland floods around 60,000 claims representing around \$2.4 billion, Victorian storms 50,000 claims and more than \$400 million, and then again at Christmas another \$700 million in storm claims. And that's not the complete list.

That \$5 billion is only from the natural disasters and catastrophes and excludes the day to day claims from car collisions, home fires and smaller storm events and the like that take that figure up to around \$20 billion in claims payments every year.

Across the Tasman where IAG is New Zealand's largest insurer – the damage bill from the NZ earthquakes has now topped \$20 billion alone.

If you extend that out across Oceania last year our part of the world contributed 17% of the entire world's insured losses – until last year that number had averaged just three per-cent for the proceeding thirty years.

It is fair to say the combined impact of all this has tested and challenged our industry but I am confident - assessed objectively –our performance has been sound. Indeed, it is the difficult years like the past one that lead me to be very optimistic about the industry's future and underscores its ongoing importance. Let me also say that I'm proud of the role that IAG has played in the industry and indeed the way that our people have selflessly assisted our customers in their time of need, often at times of significant personal distress. It's easy to forget that insurance company employees are also members of our community and that they are also affected when events hit or when disaster strikes.

IN THE SPOTLIGHT

In the wake of the worst year on record for natural disasters the performance of insurance companies is rightly placed in the spotlight.

In the aftermath the industry was the subject of no less than ten government reviews and inquiries – many of which are ongoing – and a record for my time in the industry.

I do not for a minute suggest the industry is above scrutiny. The industry should absolutely be accountable for its actions and it is right that our policies, practices and customer outcomes are visible for all to see. As an industry we willingly take on board constructive suggestions as to how we can better meet the needs of all our stakeholders.

Indeed, one outcome of the Queensland floods is the introduction of a common definition of the term flood across all insurers to help assist customers' understanding and certainty around cover. All insurers have traditionally used their own definitions which in turn impacts how an insurer assesses a particular event. This common definition was something called for by the industry back in 2008 but denied at the time by the ACCC after lobbying from consumer groups who feared collusion. I find it interesting that those same consumer groups are now calling for a common definition and for greater transparency around the extent of coverage. Sometimes out of adversity comes sensible change.

Another welcome outcome is the pending introduction of one page key fact sheets to appear at the start of product disclosure statements to improve consumer understanding of the product. Any initiatives that improve understanding while preserving the rigour around the insurance contract are undoubtedly helpful.

What is less than helpful is commentary that simply distorts the reality of the situation at hand, or plays for political point scoring. This is sometimes an

unfortunate but successful deflection technique by those who have allowed building on flood plains or other disaster prone areas and failed to adequately protect the community and our way of life through prudent mitigation initiatives which would either prevent the event from occurring in the first place or minimise the damage and hardship when an event does occur.

Often having a calm public conversation about the insurance industry and its performance can be difficult as these topics only tend to receive focus after a catastrophe when understandably emotion is high. At these times facts, figures and objective analysis can take second place to individual loss and our human instinct for compassion, as well as the natural desire to want to allocate blame.

NOT PAYING CLAIMS

The perennial criticism of the industry is that it somehow doesn't want to do the job it's tasked with and has an unwillingness to pay claims.

This is just nonsense.

Paying claims is what we do. It is our core business.

The financial ombudsman reports 98% of insurance claims are paid without dispute.

We also know that customers who make a claim have higher levels of satisfaction and are more likely to stay with us longer term. It is our moment of truth and any suggestion that insurers don't look to pay legitimate claims is simply wrong.

People's perception of insurer performance in this regard is no doubt fuelled by the commentary they hear. Some recent research we conducted revealed that 16% of consumers don't trust insurers to pay claims. That's almost one in five, a number that concerns me greatly and one that the industry needs to address.

However, that sort of statistic becomes more understandable if we look at the Queensland floods for instance. Even if you only took a passing interest in the topic you would be left with the impression that insurers – including some of our brands - don't pay claims.

The storms and flooding started in December 2010 and forced the evacuation of thousands of people from scores of towns and cities while three-quarters of the state of Queensland was declared a disaster zone. Communities along the Fitzroy and Burnett Rivers were particularly hard hit and an unexpected flash flood raced through Toowoomba's central business district - water from the same storm devastating communities in the Lockyer Valley soon after. A few days later thousands of houses in Ipswich and Brisbane were inundated as the Brisbane River rose.

Our businesses immediately swung into action and began assessing claims, cleaning homes and rebuilding lives. Homes in Toowoomba and Lockyer Valley covered under our storm water runoff provisions – thousands of claims paid.

IAG brands paid all claims in accordance with the policy terms and conditions of the policy bought by the customer. Even under policies that had a clear flood exclusion more than 70% of claims were able to be paid as determined by independent expert hydrologists.

But where it was clearly flood we - and most other companies - were unable to pay. It was a particularly difficult time to be an insurer; no one wants to find themselves in the position where they are unable to help. However, we also owe it to our other policyholders, to our shareholders and to the community at large to only pay legitimate claims. Indeed where there is doubt about the legitimacy of a claim, it has been my experience that insurance companies tend to err on the side of the consumer.

Very soon the industry encountered the predictable calls to pay flood claims on insurance policies that did not offer flood cover. While understandable and forgivable from customers and inevitably replayed in media, people in any level of government should know better and knee –jerk calls for insurers to pay for an event that they had not been collecting premium for were reckless and politically expedient.

Reckless in two ways. Uncovered payouts on large events present a solvency issue for insurers which places all insurance customers in danger. Second, how could an insurer accept these claims just because the scale of this event was large and received so much media and community attention? How was a Brisbane flood claim different to the customers who were denied flood claims in the many other flood events which had preceded them?

Examined as a standalone proposition it is also quite curious. I am unsure of another example whereby government would think it reasonable or appropriate to demand that a private business supply goods and services that had not been bought or paid for.

I recently was very fortunate to interview one of the world's most respected investors Warren Buffet and I asked him about this very matter. He put it

simply that an insurance company is not a charitable organisation, it is an organisation that makes promises and keeps them. If something falls outside of those promises it may be that society decides that society should pay and the government should step in. In that case, the cost is being spread across all taxpayers, but the idea that shareholders only should be the designated relief organisation does not make sense.

Customer research also supports the decision. More than half agree or strongly agree that insurers should not pay claims which are clearly not covered by the policy. Our challenge - to explain to the 12% who disagree why insurers are unable to do this. With the passing of time, and considered reflection, I am hopeful more people may understand and appreciate the rationale for our decision.

Fortunately, the flood issue is well on the way to being fixed with flood mapping being expedited by all levels of government. Mapping that has meant insurers now have a clearer view of where the flood risk is located so they can price and deliver a flood product to those communities. IAG brands now offer flood coverage nationally and now more than 80% of home buildings policies in Australia cover flood.

DELAYING CLAIMS

Another suggestion is that insurers intentionally delay the payment of claims so they can continue to accrue interest on these monies.

This has most recently surfaced in New Zealand in response to the devastating earthquakes.

Yes, it is true the rebuild continues in Christchurch, for good reason. Most natural disasters have a timeframe then they are over and recovery begins. A storm may last an hour, a bushfire some days, a flood some weeks but they all have defined start and end points.

An earthquake is very different. It is still happening – it is the equivalent of a town having been burning for more than a year. Just a few weeks ago we saw another 5.2 earthquake that required evacuations in the city – it was just one of the more than 11,000 aftershocks that have rocked the community. While we have made good progress it is impossible to rebuild homes when the ground is still moving. Also in many instances the earth movement is so bad there is nothing to build homes on. If you picture opening your front door and experiencing a 1 metre drop to ground you start to get the picture. That means all insurers are working co-operatively with government as plots of land are either deemed safe to build on or not. Unquestionably a process that takes longer than anyone would like, but one that is an unfortunate necessity.

We could just cash settle claims and leave customers to their devices, and in some cases at the customers' behest we will, but we think we have a moral obligation to rebuild communities rather than leave a ghost town.

And as for accruing interest on claims money as a result of this process, from a business perspective it makes more sense to get these liabilities off your books – not hold onto them.

WHAT CAN THE INDUSTRY DO

So, it is clear that as an industry we have some work to.

Some priorities for us must be:

Getting better at telling our story. Today is just one small part of that and I know the Insurance Council of Australia is looking at how the industry's important role can be more clearly communicated. But it is not just up to the industry body to have a voice. I think anyone who works in the industry knows its intent and the good it does, and I challenge us all to be advocates at all opportunities.

Product disclosures. We know we need to be explicit about what our products cover and what they don't. Consumer understanding is key. We have had Product Disclosure statements reviewed by language experts and made significant changes. We are always open to considering further such initiatives. This includes placing bi-lingual staff in certain branch locations and customer advocacy and education as part of media campaigns and in renewal documentation.

But at the end of the day as we all know the only way to get respect is to earn it – not demand it.

That means being transparent and accountable with customers and stakeholders. It means doing what we say we will do. It means having the right products in market and acting with integrity at claims time. I think we equip ourselves well on all those measures, but we can always improve.

CONCLUSION

In conclusion the Australian insurance industry is strong and robust and in an environment of growing risks and natural disasters – it is more important than ever before.

As I've said:

- The industry pays more than \$80 million dollars every day.
- It pays 98% of all claims without dispute.
- It does economic good – it is an economic shock absorber and nation builder.
- It does social good - it protects the taxpayer who would otherwise be footing the bill following disaster and protects individual wealth.
- It does mental good - it gives peace of mind as well as supports individuals in their toughest times of loss and potentially grief.

But mostly, I hope you leave here with a greater appreciation of the insurance product and the value you get from it every day. And if you decide you want to camp out in front of our branches anytime soon - that would be ok too.

