Australian Government | Australian Small Business and Family Enterprise Ombudsman

Report Overview

October 2021

The Show Must Go On: Is a discretionary mutual fund the solution to the insurance crisis facing Australia's amusement, leisure, and recreation sector?

Background

- The Australian Small Business and Family Enterprise Ombudsman (ASBFEO) conducted a self-generated inquiry in 2020 into the insurance market for small business, finding significant dysfunction for several sectors.
- The Amusement, Leisure, and Recreation Association (AALARA) submitted to that review noting that many members were facing closure and/or stranded assets due to the unavailability of insurance.
- AALARA then approached the Federal Government to seek support to establish a discretionary mutual fund (DMF).

Preliminary findings

- A DMF suits the industry represented by AALARA.
- A DMF may be a suitable way to address the current insurance crisis facing the industry.
- The suitability and durability of a DMF solution for the sector will depend heavily on:
    - support for legislative reform from states and territories, and willingness to accept the solution by councils and land/showground managers.
    - The final makeup of the membership.
    - The cost of premiums and reinsurance, the management of the DMF and any management costs, and the size of any claims in the first years of operation.

About Discretionary Mutual Funds (DMFs)

- DMFs operate to provide risk cover on a discretionary basis to a group of individuals or organisations, through a 'Certificate of Protection'.
- DMFs do <u>not</u> offer an insurance product:
    - Under traditional insurance coverage, a policy holder has a contractual right to have their claim paid upon meeting the policy's terms and conditions.
    - Under DMF coverage, the DMF's members are entitled to submit a claim for indemnity to the DMF's board, which may or may not approve the claim, at its discretion.

Benefits of a DMF

- DMFs are often created to address market failure or significant dysfunction.
- DMF members are accepted or rejected by the Directors, who have significant industry knowledge, allowing them to more closely monitor risk profiles of those covered.
- DMF membership can also be predicated on compliance with a range of risk management and training protocols to lessen the risk profile across the membership.
- Because DMFs do not have shareholders to make returns to, they are able to operate on slim margins, potentially reducing costs to members.

- DMFs can offer additional services to their members, adding value over the protection offered.

Challenges

- The DMF should be fully funded for the first year, requiring a reasonable amount of start up capital.
- Many pieces of state, territory, and local government legislation and regulation require businesses operating on their land to hold insurance, which a DMF cannot offer.
  - To address this, these pieces of legislation and regulation could be amended to allow membership of a DMF in lieu of insurance where insurance is not available, or the market is significantly dysfunctional.
- A DMF should be established in such a way to ensure its ongoing durability.
- Consumers may have concerns about the discretionary nature of coverage.

Alternatives

- A range of alternative options have been considered to address this issue, including a captive, self-insurance, group insurance schemes, a reinsurance pool, tort reform to address risks (‘the New Zealand solution’), implementation of a National Injury Insurance Scheme, and hybrid models.
- A recent entrant to the market has been Coversure, a respected UK-based insurer:
  - Only provides $10million coverage (half of the $20million required by most legislation/regulation).
  - Industry is reporting premiums of at least double that they were previously paying.
  - Will not cover the whole market.