Marsh

ASBFEO Enquiry
“The Show Must Go On”

Submission: Marsh Australia

November 2021

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Introduction

Marsh appreciates the opportunity to provide input to the Consultation Questions raised in the ASBFEO report on the proposed Mutual structures for the Australian Entertainment Industry. Against a backdrop of increasing costs of insurance, the challenges faced with obtaining adequate protection and with new emerging risks on the horizon, we recognise that now is the right time to reset and innovate.

Marsh's History with Discretionary Trusts (DT)

Marsh, through its subsidiary JLT Risk Solutions, has a long history of assisting businesses small and large as well as local government councils in their risk financing needs through Discretionary Trust structures. Marsh currently manages more than 40 Discretionary Trust schemes in Australia with in excess of 400,000 members.

In our Discretionary Trusts, businesses or organisations with similar insurance needs pool their coverage needs together to create a mutual self-insurance pool with excess insurance wrapping around it. This is useful for liabilities where associations and business groups share or are exposed to similar risks. There is no right to have a claim paid as the Trustee has the sole discretion to consider a claim and pay it.

Our view on the development of markets for AALARA and the sector

AALARA and its associated businesses will continue to be subjected to vast market fluctuations for both availability of adequate insurance coverage and affordability of associated insurance premiums.

Whilst we believe that a Discretionary Mutual or Trust structure will be of benefit, it will require substantial support from Government over the medium to long-term plus a substantial investment in ancillary risk management measures to improve the risks associated with the sector.

Maintaining consisting membership numbers through the formative years of the Mutual structure will be of utmost importance to sustain a financial model that benefits the industry. Any large fluctuations through a lack of commitment from members will result in additional support being required to maintain the Mutual as a going concern.

We provide our considerations to the questions raised in the report and will be happy to support AALARA and ASBFEO in their endeavours to establish a solution that will be sustainable into the future.

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Input to Consultation Questions

Consultation Questions	Our Comments and Suggestions
1. Is there a need for action by government? Is there a proven incapacity for the industry to self-support a solution?	It is our opinion that two major changes are needed with respect to liability insurance for the sector: a. premium contributions need to increase to address claims exposure; and b. claims deductibles need to increase to encourage insurers to reconsider their participation on liability risks for the sector. The current challenges are not something that can be overcome with only a modest increase in costs. Passing on the full cost of rectifying the problem would likely destroy many industry operators. We don't believe that the industry is able to self-support the required financial impost in transitioning to a sustainable solution, and government assistance would give the industry the best chance of a positive outcome. Historically, general liability insurance for the sector has been almost exclusively underwritten by various syndicates based in Lloyds of London. Over the past few years, the sector's performance has come under increased scrutiny due to the general poor performance of the Lloyds market, and the requirement of syndicates to stop deploying capital to poor performing risks. Across the broking fraternity in Australia, it is a long-held opinion that the premiums being contributed by these industries has been insufficient when rated against claims frequency and severity. This is evidenced by the widespread inability of non-Lloyds insurers to compete on price. Additionally, a significant challenge is the comparatively low claims deductibles that liability policies across the sector incur. This is driven by the need to keep deductibles affordable to the policyholder, however the result is fewer market participants and the inability of some of the world's largest liability insurers to participate on leisure and amusement risks.
2. If the government does not act to support the sector, what alternatives could the sector pursue?	The sector's biggest challenge is the lack of underwriting markets willing to support their risk. The sector could explore models that encourage insurers to underwrite risks through higher self-insured retentions and a more diligent and demonstrable approach to risk management.

	Many insurers continue to view the sector as an industry where claims are inevitable. The nature of activities, and the operation of certain civil liability legislation across the states and territories, means that a level of claims activity is inevitable for any insurer who participates in this market.
3. Are there any other groups or entities likely to be affected if the government does not take action?	Amusement ride operators, adventure parks & adventure ride operators, caravan parks, holiday cabins, children's play centres, tour operators, skirmish/paintball operators, stunt schools, animal related activities (e.g. petting zoos, horse-riding), pyrotechnics operators & trampoline centres are some examples of groups within the broader entertainment & leisure sector that will be adversely affected without government intervention.
4. Are there any other options for action that should be considered by the sector or the government?	The sector may need to take on a greater portion of risk than it currently does, and/or pay a higher financial impost for the transfer of that risk on to the insurance market. This may come in the form of; increased premiums, higher deductibles and excluded activities. Improvements to minimum standards of best practice; third party risk assessments, industry body accreditation, facility improvements & staff training, may require further development and implementation.
5. What other aspects of DMF better practice should be considered?	DMF's or Discretionary Trusts can voluntarily employ the same or similar compliance and best practice rules as regulated insurance companies. In our experience of successfully managing more than 40 Discretionary Trusts for more than 400,000 members across many and varied industries, we have refined and enhanced administrative practices to apply sound processes (including actuarial, underwriting, claims, legal and accounting) amounting to a sound, compliant and practical governance framework without some of the regulatory burdens applicable to regulated insurers.
6. Are the public policy considerations listed accurate? Should additional considerations be included?	No further suggestions
7. Is there sufficient evidence that a DMF, if appropriately formed and governed, could work for the various stakeholder groups?	There are a number of operational examples of where a DMF or comparable model has been implemented in order to secure coverage not available through conventional channels. While the performance of every DMF will vary, if the establishment of the vehicle is undertaken with diligence and if the policy settings are balanced between indemnifying member loss without absolutely burning supporting underwriters, the foundation of the DMF model is resilient and can deliver ongoing benefit to industry and other stakeholders. Above all else, the primary function of a DMF is to address the smaller and expected claims from a risk or group of risks. This adequately distances the insurance market from frequency losses to a degree where strong competition amongst underwriters for premium can resume.

8. Are there other regulatory considerations that should be addressed?	Consideration should be given to the fact whether any regulations imposed to DMF's or other Discretionary vehicles through APRA would be detrimental to their existence and cost basis. It could well be that in the case where DMF's are subjected to APRA regulations, community organisations currently utilising Discretionary structures would be disadvantaged and pushed out of solutions that are currently working well in a "non-APRA regulated" environment. Absent of meaningful exemptions under APRA regulations, organisations would rather consider establishing Captives or Cell Captives offshore.
9. Are the design, risk management, and governance suggestions appropriate?	Yes, if the final structure is a DMF (company limited by guarantee), then the design etc. is appropriate.
10. Does the timeline appear reasonable?	The suggested timeline of three to six months to establish the final structure is not a problem. The placement of the re-insurance risk, both on a per claim and aggregate basis, would be expected to take 3 months from the time that all relevant underwriting information is available for market. This includes claims, industry demographic and financial information, risk management information, as well as details concerning the operation of the DMF and how membership may be administered. Given the above comments it will, in our experience, take more time than three to six months to align and consult with stakeholders, insurance industry experts and government and gather all the information required to secure the re/insurance solution to support the Discretionary structure. With an industry DMF likely to involve hundreds of members across various segments, a timeframe of up to nine months would be more likely.
11. Are there alternative examples of government intervention that should be considered?	The model outlined in the report appears reasonable, however the quantum and duration of government support are key items of consideration. The interim report indicates that a level of temporary support is the preferred model – however, liability insurance is notoriously "long-tail", with claims lodged by third parties on average more than four years after the original incident. We would anticipate even longer delays in formal lodgement of claims for this industry – with a substantial proportion of claimants likely to be minors, the length of time between an incident causing injury, and formal notice of claim, could comfortably exceed a decade in some cases. Importantly, under a DMF, the Fund is "renewed" every year, and contributions re-committed in full. DMF's become self-supporting at the time when surplus funds from prior periods can be released and contributed back into current models – however, this relies on re-insurance agreement to then accept the exposure borne by the DMF (i.e. they "drop-down" to a lower claim attachment point, reducing the liability of the fund for any further claim to nil).

	When considering a public liability DMF for this industry, it may be a requirement of underwriters for funds to be held for a period of 8-10 years before being released for re-investment.
12. Are there other aspects that should be considered in terms of market conditions or capacity building for the DMF board and membership?	No comment.
13. What alternative models of financial support could be offered?	With one of the greatest imposts on participants being a claims deductible of at least $20-$25,000 for most leisure risks, the ability for Government or other funding to address the claims excess could be considered – however, this could lead to a number of frivolous claims at an under-deductible level. Premium financing options for industry could be considered, however this would not address the challenge of either higher premiums, or higher deductibles payable at a time of loss. The most drastic model would be considering full indemnification for industry participants. This would be expensive and potentially do very little to address risk concerns across the segment. It would also potentially create a dangerous precedent if other industries were to find themselves in a comparable predicament in future.
14. Are the governance and reporting proposals appropriate? Is the suggested board make-up likely to provide the best results for the DMF?	Governance, reporting proposals and suggested make-up of the board are appropriate for a DMF. A board member who had some experience at a for-profit insurer should not be disqualified per se if they bring a deep understanding of mutual and/or other self-insurance structures to the board.
15. Are there other issues that need to be considered in relation to interaction with states and territories? a. Are the perceptions around discretion presented accurate? Are there other perceptions that should be considered? b. Are there specific legislative barriers that should be considered?	Perceptions about discretionary nature of claims consideration and payment are accurate and we agree that the discretionary element is normally considered an advantage by members in our Discretionary Trusts. However, insurers providing the excess coverage to Discretionary Mutuals and Trusts are sometimes suspicious about the discretion a board or Trustee can apply to claims being considered as they are counting towards exhaustion of the per event or aggregate attachment points of excess insurance. Therefore sound analytical and actuarial model needs to be employed by any discretionary structure to set attachment points for insurers at a level where they feel comfortable to support the structure.
16. Are the current safety standards/regulatory environment/Quality Assurance verification purposes fit for purpose? If not, how would you suggest these be amended?	No comment
17. What needs to be undertaken to ensure consumer awareness around the DMF? Are there alternative methods for consumers to manage their own risk?	Practically, from a consumer/service-user perspective there is no change to a conventional insurance policy maintained by the business. Additionally, the safety warnings and public information systems currently in place are not impacted, and remain in place.

	The DMF may create opportunities to focus on the risk management approach of participating members. This could be a positive if a risk framework was implemented for DMF members that could be actively promoted to consumers as part of their service or facility use.
18. Are there other sectors that should be included in membership of this DMF?	Potentially. Further investigation would be required.
19. Are the proposed DMF member entry requirements adequate? What additional requirements could be considered?	We consider the member entry requirements as adequate.
20. What else should be considered in the process of the final proposal development?	Premature to comment comprehensively on the final proposal, however the period of required support is key. Unless there is a commitment to provide funding for a period of 8-10 years (to address the latent claims reporting risk outlined above), any DMF model is more likely to deliver short of expectations.
21. Are the key success features identified accurate? Are there other features that should be considered?	Critical to the DMF's success will be the development of initiatives that will look to have members commit for a minimum membership period. This reinforces the importance of longer term commitment of financial support – underwriting markets will start to re-enter the segment over the next 3-7 years. If the full cost of the DMF model is transferred on to the industry at this time, a "two-speed" market will emerge – one for those who are lower risk and able to take advantage of capacity re-entering the market, and a harder market for claims impacted or higher risk activities. The intent has to be for a DMF to become self-sustaining, but in our opinion for a liability risk that can take a period of up to a decade.
22. What other offerings to the DMF membership might increase 'stickability'?	By appointing a broker to arrange the relevant insurance protection supporting the DMF, the ability exists to provide additional insurance products and risk management services to clients under a consistent banner. Business property and interruption insurance, financial risks insurance, cyber, plant and equipment, workers' compensation, commercial motor and domestic lines could all be offered to increase the level of engagement between the member and the managing broker.
23. How important is contestability of service offerings? Are there other ways to ensure contestability?	Contestability is key, and the role of the DMF and the insurance broker is to create a risk environment where competition is created between insurers. This can be achieved on a portfolio basis (i.e. a panel of insurers underwriting all risks on a proportionate basis), or a per-risk basis (i.e. individual risks within the DMF are broked to select insurers). Additionally, within the DMF a model should exist to provide purchasing options to members. The simplest examples are limits of cover, and level of claim excess retained by the member.

24. What are additional best practice claims handling procedures?	The best claims handling processes combine efficient handling, along with controls that anticipate losses and reduce frequency. Consistency in handling, through both disciplined processes and a steady team of claims managers, create an environment where trends can be identified, and controls and policy structures adjusted accordingly before losses accumulate to a catastrophic level. Empowerment of relevant claims staff is essential, with the need for them to have adequate authority to take decisive early action to reduce claims costs.
25. Should the DMF include a constitutional protection against demutualisation? Should government introduce a protection against demutualisation for the broader sector?	Not in our opinion. We do not view the proposed DMF as comparable to the NRMA or any other large insurance or banking mutual.
26. Is public confidence in the DMF likely to be an issue? What else could be done to encourage public confidence in the proposed DMF?	In our opinion, it is unlikely that public confidence will be an issue. Our firm currently manages a substantial number of Discretionary Trusts with a membership of in excess of 400,000 members and there have never been concerns raised about their stability or ability to pay losses. Importantly, a key item of a DMF is a requirement for there to be no exposed capital risk. This is a very strong argument against any public confidence issues that may arise.
27. Are there appropriate mechanisms to reengage with private sector/industry market solutions over the life of the insurance market cycle? If not, what proposal settings would enable the sector to take advantage of a softening market?	This question reinforces the role of an insurance broker in this process. The broker can monitor market conditions and DMF performance and recommend changes to the operation of the DMF accordingly to ensure that best value continues to be delivered to members. With a DMF running for a defined period (usually 12 months and renewed annually), as market conditions change the broker works with the DMF board to ensure member needs are met and best interests served. From the outset, we would expect the liability market to remain in a relatively hard phase for at least the next 2-3 years, especially for high risk activities. It is our opinion that while price and capacity pressure will ease in time, it is highly unlikely that capacity will return to a point where premiums and coverage for this sector is comparable to the levels seen 5-10 years ago.

Marsh's Capability and Experience

Alternative Risk Transfer Solutions

Marsh currently manages over 1,500 Alternative Risk Transfer and Financing vehicles worldwide to support or replace traditional insurance placements. Below is a brief overview of Marsh's relevant experience and capabilities specific to the distinctively Australian Discretionary Trusts (which are very similar to a Discretionary Mutual Fund).

Marsh's History with Discretionary Trusts (DT)

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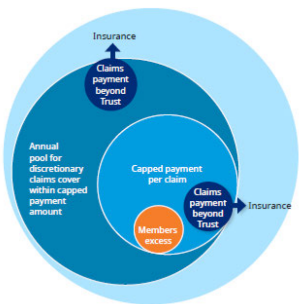
Concept example



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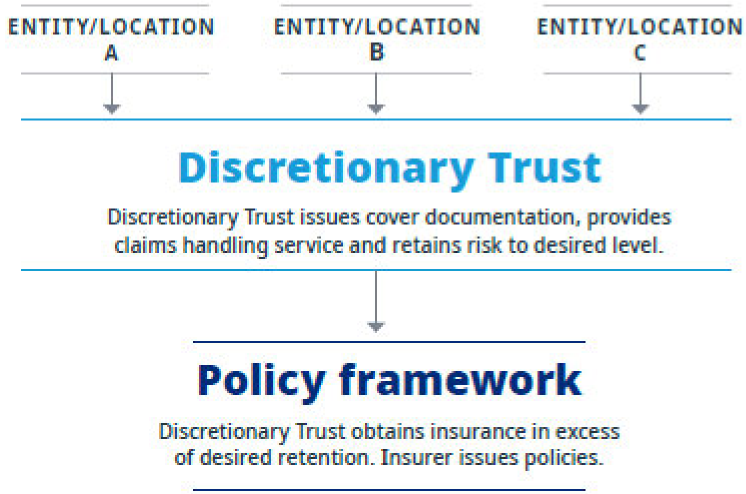
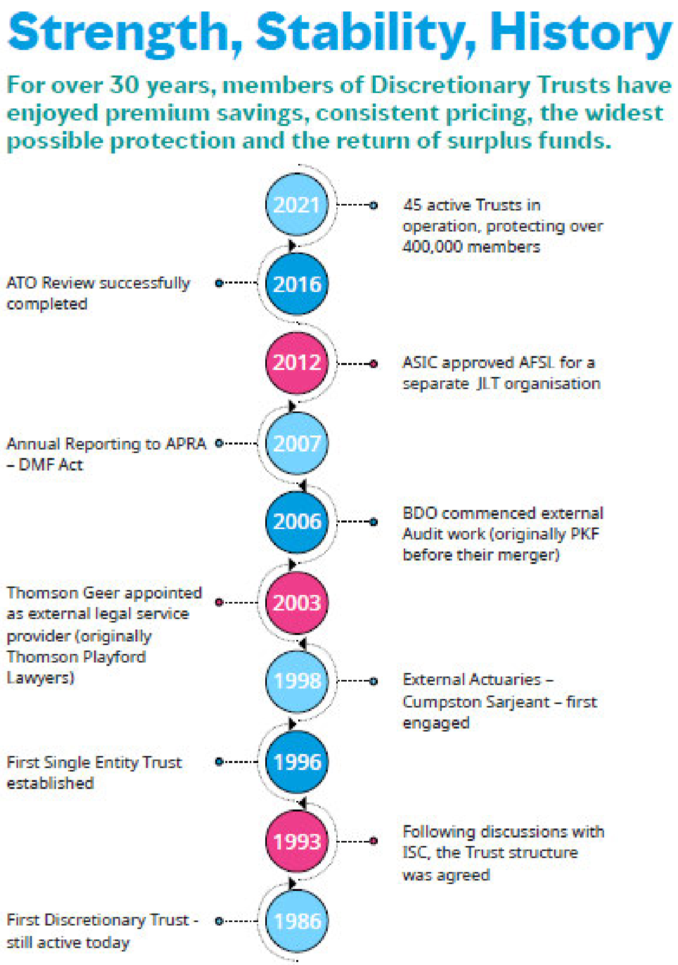


A Legal Framework that has stood the test of time

- Marsh/JLT Discretionary Trusts are managed investment schemes and are subject to the reporting and product disclosure requirements with ASIC under the Corporations ACT 2001
- Marsh/JLT hold an exemption from Registered Managed Investment Scheme requirements of the Corporations Act 2001 (section 601ED)
- Each Discretionary Trust is registered with an individual Australian Business Number (ABN) and Tax File Number (TFN)
- Each Discretionary Trust has its funds in a separate bank account with a large Australian Bank, funds are held in the Trust’s name, entirely segregated and shielded from cross-contamination by any other Discretionary Trust
- Each Discretionary Trust is independently audited each year by BDO, who also act as the Tax Agent for the Trust
- Each Discretionary Trust is operated in accordance with its own separate Trust Deed and Scheme Rules
- The Trustee is required to consider claims made by the members of the Discretionary Trust, whether or not the event is covered by any conventional insurance taken out by the Discretionary Trust
- The payment of such claims, which are not covered by the conventional insurance component, is subject to the Trustee’s discretion
- The Trustee is bound by the trust deed and can only apply member contributions for the specific purposes of the Discretionary Trust



About Marsh: Marsh is the world's leading insurance broker and risk advisor. With around 40,000 colleagues operating in more than 130 countries, Marsh serves commercial and individual clients with data-driven risk solutions and advisory services. Marsh is a business of Marsh McLennan (NYSE: MMC), the world's leading professional services firm in the areas of risk, strategy and people. With annual revenue over $17 billion, Marsh McLennan helps clients navigate an increasingly dynamic and complex environment through four market-leading businesses: Marsh, Guy Carpenter, Mercer and Oliver Wyman. For more information, visit mmc.com, follow us on LinkedIn and Twitter or subscribe to BRINK.