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# Private Insurance Market

Submission to the Insurance Council of Australia's  
Strategic Review of Commercial Insurance

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June 2021



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Private Insurance Market: Submission to the Insurance Council of Australia's Strategic Review of Commercial Insurance

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# Introduction

Engineers Australia thanks the Insurance Council of Australia (ICA) for the opportunity to make a submission in response to its consultation paper *Role of the Private Insurance Market – Independent Strategic Review: Commercial Insurance*. Many of our members have been severely affected by the current hardened insurance market and have reported a range of problems associated with affordability and accessibility of both professional indemnity and public liability insurances.

The current insurance crisis is shaking the confidence of engineering businesses and putting the recovery of sectors and industries post COVID at severe risk.

Sole practitioners and Small-Medium Enterprises (SMEs) appear to be the most impacted, particularly those working in the building and construction industries and the amusement park industry.

Engineers Australia supports the need for constructive dialogue and collaboration among key stakeholders across industries and industry bodies to find sustainable solutions to the current insurance problems. The urgency and scale of the current insurance problems that the engineering profession is facing requires consideration and implementation of a range of solutions as soon as possible. To restore business confidence, industries need to recover on solid foundations, which must be underpinned by accessible and affordable insurance products.

## About Engineers Australia

With around 100,000 individual members, Engineers Australia is the profession's peak body. As the trusted voice of the profession, Engineers Australia exists to advance society through great engineering recognising that engineering plays a pivotal role in society creating healthy, prosperous, secure and sustainable communities.

Engineers Australia's high practice standards, globally recognised credentials and international agreements enable its members to live and work around the world.

We look forward to having further conversations with the ICA and to contribute to the development of coordinated implementation plans. To discuss this submission and insurance issues generally, please contact Baoying Tong, Senior Manager - Building Reform and Projects at [bytong@engineersaustralia.org.au](mailto:bytong@engineersaustralia.org.au).

# Current problems with the insurance market

Engineers Australia recognises that the problems in the current insurance market are the result of the convergence of many forces in the global insurance market, as well as other local factors. For engineers, the current situation is impacting not only the availability and affordability of insurance but in some industry sectors there has been a market failure.

## Availability and affordability of insurance

The building and construction industry and leisure and entertainment industries are critical to the recovery of the Australian economy post COVID. The pandemic has forced many engineering businesses to operate with unprecedented uncertainty. Therefore, it is imperative to formulate serious proposals and implement sound solutions before more engineering businesses are forced to cease operating.

## Building and Construction Industry

For members practicing in the building and construction industries, the impacts of the hardening insurance market have varied greatly, with structural, geotechnical, civil, fire safety and façade engineers among the most affected. The key concerns are:

- Rise of annual premiums. Multiple sources have reported premium increases up to 600% over the last 2-3 years.
- A limited number of insurers willing to provide coverage.
- Inconsistent and poorly defined policy exclusions, e.g., on coverage of cladding.
- An ongoing increase in deductibles and exclusions and a reduction of coverage level.
- Continuous pressure from clients requesting arbitrary large amounts of PII coverage with no apparent risk assessment to justify the figure.

## Amusement Park Facilities

For engineers who work on the design, construction and inspection of amusement park facilities, the fundamental issue lies in the accessibility of insurance. Engineers Australia has been informed by industry colleagues that insurers have left the industry. As a result, engineers cannot renew their policy or get new coverage. This situation threatens the rebound of the tourism industry as well as the safety of amusement park facilities.

## Effects expanding to include large firms

As the insurance crisis continues to unfold, more sectors and businesses appear to be affected. Increasingly, many large companies are reporting similar problems to the SMEs resulting in similar pressure on the availability and affordability of insurance.

# Recommended actions

## Guidance notes

To help engineering industries develop coordinated solutions, Engineers Australia strongly recommends further guidance notes be published by the ICA on an estimated timeline for improvement to the insurance market. Industries must have an understanding of the landscape of the insurance market so that actions can be developed and prioritised based on projected short/medium/long term market movement.

## Improving the risk profile of the engineering profession

Engineers Australia's focus is to reduce the total claims paid out by insurers and hence lower the risk profile of the engineering profession. The theory as represented in the formula below is based on our understanding of the link between claims and insurers' profit margins. Actions targeting each factor can reduce the size of the problem.

$$\text{Insurer's profit} = \text{Investment incomes from premiums} - \text{Total claim paid out} - \text{Overheads}$$

The total claims paid out can further be broken down according to the following formula.

$$\text{Total claim paid out} = \text{No. of claims} \times \text{Average payout size per claim}$$

Engineers Australia strongly believes actions to improve risk allocation and risk management practice will lead to the reduction of the above factors and hence reduce the size of the problem in the longer term.

## Engineers Australia's action plan

Engineers Australia has identified a range of solutions to address the current crisis and has developed an action plan covering short, medium, and long-term priorities. The plan is focused on improving risk management practices within the profession. Engineers Australia's recommended solutions and the three stages of the action plan are outlined as follows.

### Stage 1: Short term

- Forge partnerships with key stakeholders to facilitate solutions.
- Organise webinars/roundtables with the ICA and insurers to focus on the most affected engineering sectors.
- Help members gain a better understanding of the insurance market to assist them in acquiring adequate insurance.

### Stage 2: Medium term

- Work with insurers to identify key risk areas in the profession and develop risk management protocols and practice guides for practitioners.
- Encourage insurers to determine fair risk allocation and link to Engineers Australia's credentialled membership grades.

### Stage 3: Long term

- Promote a culture shift regarding risk allocation and accountability in targeted engineering industries.

## The role of government

The ICA paper suggests that no direct intervention by the government be considered until all other options have failed. While appreciating the standpoint in general, Engineers Australia recommends early government intervention in sectors such as the amusement park industry where the lack of insurers' appetite has threatened the viability of almost all engineering firms in the industry. Prompt government intervention is imperative for the industry to survive.

For most other industries that are experiencing issues with affordability rather than availability, government should still play the role as the facilitator. To accelerate the decision-making process and ensure a holistic, consistent problem-solving approach, government must step up and take more ownership to lead the conversations, together with the ICA and others. This is especially so for sharing and promoting good risk management practice across industries.

As there is rapid change and regulatory and policy reforms happening in many jurisdictions, especially in the building and construction sector, it is important to ensure that any reform proposals consider potential adverse effects on insurance. Engineers Australia has flagged this issue to governments during the development of their reforms and encourages them to proactively monitor and evaluate the consequences of regulatory reforms on insurance.

Lastly, as clients on projects, governments should re-assess internal risk management systems as some industries have seen government clients impose excessive levels of PII. The numbers being provided to Engineers Australia appear to be arbitrary and based on a 'cookie cutter' approach with no sign of serious risk calculations. The consequences from such behavior have both short- term and long term-impacts on the industries, which include:

#### Short term:

- Adverse impact on competition as many companies (SMEs in particular) cannot comply with the required coverage.
- Transfer of unsubstantiated risks to the private sector which forces participants to be exposed to unnecessary claims.

**Long term:**

- Exacerbates the litigious nature of certain industries, such as the construction industry.
- As the PI insurance claim pool is shrinking in size, additional insurance commitment to new projects will reduce the size of this pool even further.

If the insurance problem cannot be resolved in time, many sectors where engineers practice, especially those that are niche but critical, will see the exit of practitioners and businesses and a loss of knowledge. This may inevitably lead to bigger crises with government having to take reactive action at a much higher cost.

Together with our industry peers, Engineers Australia is actively seeking to engage with relevant government bodies on this point.

# Comments on options proposed in the ICA consultation paper

Engineers Australia supports the four key areas of focus (namely, affordability, availability, market failure and government intervention) highlighted in the ICA Consultation Paper. Engineers Australia's comments on the sixteen proposed options in the consultation paper are set out in the following table.

Engineers Australia has assigned a ranking from 1-5 for each of the options in the Consultation Paper. The options with a higher ranking reflect the options of most immediate concern to the engineering profession. As the situation changes, the options with low scores may be adjusted accordingly.

Item No. from the paper	Name	Ranking	Engineers Australia Comments
15	Collaboration with governments to reduce regulatory barriers	5.0	<p>Engineers Australia notes that this is of vital importance. Government regulations may create unintended barriers that ultimately increase the magnitude of an insured's risk to an extent that no insurer is able to cover. For example, the NSW Design and Building Practitioners Act 2020 introduced the extended duty of care (part 4) provision that applies retrospectively to projects completed in the past 10 years. The intention is to better protect consumer interest. Many insurers have found it impossible to calculate the additional risk and hence have excluded any coverage from this part. This did not achieve the intended original aim of the clause.</p> <p>As many industries are facing significant pressure to access affordable insurance, governments must pay attention to the market's voice and understand any impacts on the insurance market before proceeding with new legislated requirements.</p>
2	Advice and education on risk mitigation	4.7	<p>Risk mitigation practice of SMEs is one of the critical factors that contribute to the risk profile of an industry. Insurers believe business owners have the best knowledge of their business risks. Anecdotally companies that can demonstrate to their insurers good contracts review/risk management/record keeping practices usually have easier conversations when renewing policies, especially during a hard insurance cycle. Anecdotally, not many SMEs appear to understand the value of this investment and industry risk management practices vary. Engineers Australia is committed to helping its members improve their risk management practices and would like to collaborate with the ICA and other insurers to develop appropriate training packages, as well as to provide advice to promote best practice for risk management</p>
5	Risk management and risk mitigation	4.7	<p>Please refer to our comments on Option 2. Furthermore, Engineers Australia notes the importance of good communication and understanding on the insurer's side. However, any proposals on risk management and risk mitigation need to address the issue from the perspective of the insurer, the practitioner and the industry body.</p>
11	Supporting the public interest - the industry's social licence	4.7	<p>Engineers Australia supports this option as it may lead to a culture shift in the insurance market. However, it is only a long-term prospect as the goal is equally driven by the commercial imperatives/economic focus of the insurance industry.</p>
4	Greater use of deductibles and coverage limits	4.3	<p>Engineers Australia agrees with this option. However, on coverage limit, it is critical to note that a change of behaviour on the clients' side must be encouraged. Engineering consultants typically do not have the bargaining power with their</p>

Item No. from the paper	Name	Ranking	Engineers Australia Comments
			<p>potential clients and Engineers Australia has seen many cases where the client required PII coverage that is disproportionate to the services fee. A recent case has seen a public sector client ask the consultant to provide \$10m PII for a \$15k fee project. Many other examples from members have indicated that on the client side, irrespective of the size of the fee, excessive PII coverages are arbitrarily inserted into contracts with no substantiating risk calculations. It is difficult to persuade clients to change behaviours, especially in a competitive market environment such as engineering consulting services. However, if the industries do not push for the change from upstream, the unnecessary risk exposures to businesses and insurers are likely to continue, as will the litigious nature of many industries. Collaboration of industry bodies is the key and Engineers Australia is willing to initiate and contribute to the conversation.</p>
8	Group captives and discretionary mutual funds (DMFs)	4.0	<p>This option is imperative for industries such as amusement parks where the availability of insurance is the biggest challenge. Engineers Australia suggests collaboration between the relevant government departments, industry bodies and insurers to develop proposals and plans given the urgency of the situation in those industries.</p>
16	Government involvement for economic benefit	4.0	<p>Before all criteria set by this paper are able to be met, government involvement is desirable given the scale and urgency of the problem. As pointed out in the consultation paper, direct intervention may not be required in all industries that are facing the issue and the priority of government intervention should be given to those that have fundamental accessibility insurance issues. Many industries are having direct conversations with the corresponding government departments. Although only limited actions have been taken by governments so far, the conversations have helped governments understand the bleak situations paving the way for further government involvement. For most industries, direct government intervention may not happen soon. Government departments should act as the facilitators for those conversations and bring all the stakeholders on board.</p>
7	More underwriting agencies with specialist capabilities	3.7	<p>Engineers Australia supports the proposal. Underwriters typically do not have detailed knowledge of various disciplines within an industry sector and hence do not always understand the difference between 'good' risk and 'bad' risk. For example, a lack of specialist knowledge within the amusement park industry is contributing to insurers' reluctance to take any risk. For the construction industry, this has led to exclusions which, for example, unnecessarily exclude all façade products instead of only 'non-conforming' façade products. Engineers Australia is willing to support this option and educate underwriters/underwriting agencies so that they have better knowledge of specialised engineering disciplines.</p>
9	Industry association accreditation and standards	3.5	<p>Engineers Australia agrees with this option in general and would like to emphasise the fact that at the core is integration of risk management into an industry association's professional standards framework. Qualifications and competence alone do not provide sufficient demonstration of the performance aspect of professional practice.</p>
1	Standard documentation	3.0	<p>Engineers Australia agrees with the option with no further comment.</p>
10	Broker specialisation	3.0	<p>Engineers Australia agrees with the option. Brokers provide the link between practitioners and the underwriters. The depth of their knowledge of their client's business has a direct impact on a client's access to and affordability of insurance.</p>
6	Underwriting consortia (Lloyd's style)	2.7	<p>Engineers Australia notes this option may require a concerted effort from an entire industry/profession and hence may only happen in the long term.</p>
13	The special case of business interruption insurance (BII)	1.3	<p>Engineers Australia notes that although BII has not been a focus of insurance for engineers. Given increased activities and threats in cyberspace, more attention to this product may be required in the near future.</p>

Item No. from the paper	Name	Ranking	Engineers Australia Comments
3	Brokers and their remuneration	1.0	Engineers Australia has no further comment on the option.
12	The special case of natural disasters	1.0	Engineers Australia has no further comment on the option.
14	Government taxes and charges	1.0	Engineers Australia has no further comment on the option.



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