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Committee Secretariat
Governance and Administration Select Committee
Parliament Buildings
Wellington

Emailed to: ga@parliament.govt.nz

Dear Committee Members,

ICNZ submission on Fire and Emergency New Zealand (Levy) Amendment Bill

Thank you for the opportunity to submit on the *Fire and Emergency New Zealand (Levy) Amendment Bill* ("Bill"), which was introduced to Parliament on 31 October 2018. ICNZ represents general insurers that insure about 95 percent of the New Zealand general insurance market, including about a trillion dollars' worth of New Zealand property and liabilities.

We wish to appear before the Committee to speak to our submission.

Please contact Andrew Saunders (andrew@icnz.org.nz or 04 914 2224) if you have any questions on our submission or require further information.

Introduction

ICNZ generally supports the Bill and in this submission we comment further on the following three aspects of the Bill:

- commencement of the new levy regime;
- the exemption from the levy for insurance covering property that are collections in public museums, public art galleries and whare taonga; and
- the proposed changes related to the setting of the levy.

Notwithstanding ICNZ's support for the changes proposed in the Bill, ICNZ remains fundamentally opposed to funding the activities of Fire and Emergency New Zealand (FENZ) through a levy on insurance. We hold this view because the levy on insurance is inequitable and not universal, contrary to the aims of section 80 of the *Fire and Emergency New Zealand Act 2017* ("Act"), is costly to collect, complex and distortionary. Perversely the imposition of the FENZ levy on insurance discourages the uptake of insurance by making it costlier, which in turn increases the exposure of

individuals/families/businesses and ultimately government to the costs of losses and disasters.¹ It would be more appropriate to fund FENZ's activities through general taxation and/or a levy on property rates/vehicle registration.

Whilst we strongly maintain this view, and noting that the current levy system is more than adequately funding FENZ's needs, ICNZ continues to work constructively with FENZ and the Department of Internal Affairs to try and make the new levy under the Act more practical to implement and less costly to apply. Given this we welcome efforts to make the new levy regime more practicable, of which the Bill is a part.

Summary of recommendations

ICNZ makes the following recommendations on the Bill:

1. the Bill is enacted by the end of March 2019.
2. definitions for "public art gallery" and "whare taonga" are included.
3. consideration is given to ensuring the drafting of proposed new clause 25A of Schedule 1 of the Act will achieve the policy intent, which is that the proposed exemption applies to relevant insurance policies entered into or renewed from 1 July 2019.
4. the following additions are made to section 142 of the Act:
 - a. a new sub-clause (g) is added to section 142(4) providing "(g) the compliance costs for levy payers of changing the rate of the levy"; and
 - b. a new sub-section (7) is added to section 142 providing "(7) The regulations may not come into force until a day that is at least 12 months after that date on which they are made".

Commencement of new levy regime

ICNZ supports the amendments in the Bill to the commencement date for sections 80 to 140 of the Act, which provide for a new levy-based system and are currently due to come into force by 1 July 2019. As noted in the Explanatory Note to the Bill, it has become clear that it is not practical for the new levy to commence from 1 July 2019. The Bill therefore changes the default commencement date for sections 80 to 140 to 1 July 2021, with the ability for this to be brought forward to 1 July 2020 by Order in Council.

ICNZ agrees that it is imperative to move the commencement date for the new levy because the current date of 1 July 2019 would be completely impractical. The levy collection system changes that are going to be required to implement the new levy are significant. Insurers will need 15 months to design, develop and implement system changes, test those system changes and communicate with their staff brokers and customers. This work can only commence once the legislation is fully amended, regulations and operational guidelines are completed, and insurers therefore have certainty on what systems changes they will need to make.

Specific steps that need to be progressed before certainty can be achieved include consultation on the key levy design elements and proposed levy rates and a second amendment Bill to make further amendments to the Act, which include details of the new levy regime. These steps are currently

¹ This is outlined in greater detail in ICNZ's August 2016 submission on the *Fire and Emergency New Zealand Bill*, available from <https://www.icnz.org.nz/fileadmin/Assets/PDFs/ICNZ-submission-on-the-FENZ-BILL.pdf>.

expected to be progressed over the course of 2019, subject to Parliamentary prioritisation and other factors. This timing and the 15-month lead-time required for implementation suggests a mid-2021 commencement is likely to be appropriate.

Given the above factors ICNZ supports the amendments in the Bill to allow a commencement date to be set between 1 July 2020 and 1 July 2021. We look forward to engaging with Government on the most appropriate date for commencement as the regulatory changes are progressed and then finalised.

Timing of exemption for the levy on insurance covering property that are collections in public museums, public art galleries and whare taonga

We note under current policy settings, public museums and galleries pay a levy on insurance for their collections and that it is proposed in the draft *Fire and Emergency New Zealand (Levy) Regulations* (“regulations”) that these are made exempt under those regulations when new levy comes into effect. The Bill would insert this exemption into the primary legislation (new clause 25A of Schedule 1 to the Act) and implement it in advance of the other changes and the other exemptions contained in the proposed regulations. ICNZ does not have concerns with the introduction of this exemption, however, to ensure it can be workably implemented it is critical that it is clearly defined, does not apply retrospectively and an appropriate lead-time of at least 3 months is provided for implementation.

The Bill introduces a definition of “public museum” but there are no equivalent definitions of “public art gallery” or “whare taonga”. Including definitions for these in the legislation is necessary to provide greater clarity on what is, and is not, within the scope of this exemption. As the sums involved could be material and there are penalties for incorrect payment of levy, the obligations need to be unambiguous.

We understand the policy intent is that this exemption will apply from 1 July 2019 (i.e. to insurance policies that are entered into or renewed from 1 July 2019). We are however concerned that as currently drafted there could be uncertainty as to whether the proposed new clause 25A of Schedule 1 to the Act would be considered to apply from 1 July 2019, which we support, or to have applied retrospectively since 1 July 2017 given it sits in Subpart 3 of Schedule 1 to the Act that explicitly applies to a transition period between 1 July 2017 and the commencement of sections 80 to 140 of the Act. Consideration should be given to ensuring the drafting of the Bill achieves the policy intent outlined above.

It is also necessary for the Bill to be enacted at least three months before 1 July 2019 so that this exemption can be practically implemented. The process for entering into or renewing insurance policies for public museums, public art galleries and whare taonga that apply from that date will take place in the months leading up to it. Annual insurance renewals for July start being sent out 3 months before (i.e. from the beginning of April) and so insurers need certainty before then. ICNZ therefore recommends the Bill is enacted by the end of March 2019 at the latest. If it is not able to be passed by then, the implementation date for the new exemption needs to be pushed out so that there is at least a 3-month lead time, or the exemption removed from this piece of legislation.

We are mindful the Select Committee is currently not required to report back to Parliament on the Bill until 1 April 2019 and so achieving this enactment timeframe would require an earlier report back. The Bill is however short and straightforward.

Levy rate setting and changes

Having regard to compliance costs

Section 142 of the Act provides for levy rates to be regularly reviewed, generally on a three-yearly basis. Government has identified that whilst section 142(1) provides that rates can be reviewed before the end of the three-year period, it does not provide for levy rates to be put in place for a period of less than three years. We note the Bill amends section 142 to clearly provide that levy rates can be set for a period of less than three years and that it also provides that FENZ can take excesses or shortfalls of levy revenue in one period into account when setting levy rate for the next period.

ICNZ understands the rationale for these proposed changes to section 142 of the Act. It is however important that they are applied sensibly to avoid imposing excessive compliance costs. Changing the levy rate imposes the need to make system changes on insurers and intermediaries (e.g. insurance brokers) and so more frequent changes to levy rates create additional compliance costs. To minimise this, levy rates should generally be set on a 3-yearly basis and yearly changes in levy rate should be avoided. In order that appropriate regard is given to these trade-offs and the compliance costs associated with changing rates, specific criteria should be added to section 142 of the Act that reflects this. We recommend a specific addition to the Bill to achieve this below.

A predictable and appropriate period for implementing rate changes

As well as minimising the frequency of rate changes to reduce compliance costs, it is also critical that insurers are given sufficient lead time in advance of a levy rate change to make necessary system changes and undertake the other work required to implement it.

The new levy is not a simple flat-rate pass through for many customers. Accordingly, the system changes are more significant than for some other types of levies provided in other legislation. It is also more complicated compared with the current levy (because it is more broadly scoped and more complex to apply). It is particularly complicated for certain types of property, for example mixed-use multi-story buildings with multiple apartments and commercial space, because the building is usually insured under a single policy, but the levy needs to be applied differently to the residential and commercial parts of it as they are subject to different levy rate calculations. Government has also signalled that the rate for different types of property might be changed over time, further complicating the system changes required to be made in response to a rate change.

If the systems changes required to implement a levy rate change need to be rushed due to a constrained or uncertain timeframe, the costs will likely increase as will the risks of incorrect levy collection/payment. Insurers are not able to commence work until the required changes are confirmed (i.e. new regulations are made) and if the period for implementation is limited and/or not predictable in advance then it is necessary to bring in additional resources (at additional cost) and/or re-task people away from other work. It is important to bear in mind that as well as running their own businesses and meeting their customers' needs, insurers are also often implementing changes to respond to other regulatory changes or initiatives.

If instead a sufficient time period was provided for making the required changes, and particularly if that timeframe is predictable in advance, it is possible for system changes to be made through business as usual processes and alongside other systems work, reducing business impacts and costs. Given that insurers are required to collect the FENZ levy for free, need to spend time and money to do this, and are subject to penalties if they get it wrong, we consider it is entirely appropriate to at least allow a reasonable and predictable period for insurers to be able to implement any changes effectively and efficiently.

Historically changes to FENZ levy rates have been infrequent and as required and there has not been the planned three-year cycle in place as will be the case for the new levy. The period insurers have been given to make the changes required to implement a levy rate change has eventuated based on when the approvals have been made within Government. As can occur in relation to other levies, this implementation period sometimes gets shorter than planned due to delays with government decision-making processes and uncertainty as to the date of implementation often arises in parallel as a consequence of this. Notwithstanding good engagement that might be occurring with the impacted industry at the time, this uncertainty has impacts. Insurers are not able to commit resources to undertaking system changes until those changes, and the time of them commencing is confirmed, meaning there is often a period when the implementation starts to loom, but insurers are not yet able to commence the required work.

The shortest period of time that might be required for insurers to implement a rate change to the new FENZ levy in future depends on various factors related to the nature and extent of the changes, insurers' systems, the time of year and wider factors such as other regulatory changes occurring in the same period. We have engaged our members and they have indicated that depending on various factors a minimum period of up to twelve months is required.

We consider however that focussing on the minimum that could be achieved somewhat misses the point. There are costs to uncertainty on the timing that could be avoided by prescribing a process that provides a certain and reasonable time for implementation. For the following reasons we consider a minimum period between when a new FENZ levy rate is determined and when it comes into effect should be prescribed in legislation, and that the appropriate minimum period would be 12 months:

- with intermediated/broker written insurance contracts (most commercial and some personal insurance) the renewal notices go out approximately 3-months before renewal and so all systems work needs to be completed before this (e.g. for intermediated contracts commencing 1 July, insurer systems need to be ready by 1 April)² and this means a 12-month lead time is effectively only 9-months for insurers;
- it takes time to develop, implement and test the IT and other system changes to give effect to a change in levy rate and to conduct the wider related change management to ensure the levy is correctly charged to customers (e.g. internal staff training, broker communication and training, engagement with intermediaries to update the intermediaries' systems and processes, and customer communications, which is not simply a matter of informing customers that the levy has increased but involves modifying all relevant invoices, statements etc.);
- a certain period of 12-months would allow insurers to anticipate changes and build in the required systems work into regular planning cycles, rather than having to react to a rate change decision made at a previously unconfirmed time in advance of the change; and
- a prescribed timeframe would provide certainty to government agencies, FENZ and stakeholders as to when the rate setting process must be completed by and avoids a planned implementation period being eroded and made more uncertain by delays in government processes.

² The process for renewing non-intermediated (mainly residential) business is shorter (begins at least six weeks before the renewal date, or mid-May at the latest for contracts commencing from 1 July). It is however the longest lead time that is material to the appropriate minimum time period for implementation (i.e. for intermediated business).

Recommended changes to clause 6 (section 142 of the Act)

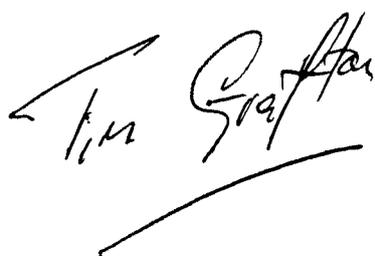
In order to give effect to the above recommendations and to appropriately minimise the impacts and costs of changes in levy rates on insurers and their customers in future, ICNZ recommends the following additions to clause 6 of the Bill (section 142 of the Act):

- a new sub-clause (g) is added to section 142(4) providing “(g) the compliance costs for levy payers of changing the rate of the levy”; and
- a new sub-section (7) is added to section 142 providing “(7) The regulations may not come into force until a day that is at least 12 months after that date on which they are made”.

Conclusion

Thank you again for the opportunity to submit on the Bill. If you have any questions, please contact our Regulatory Affairs Manager on (04) 914 2224 or by emailing andrew@icnz.org.nz.

Yours sincerely,



Tim Grafton
Chief Executive



Andrew Saunders
Regulatory Affairs Manager