NSW LEGISLATIVE COUNCIL
Inquiry into the Fire and Emergency Services Levy

Submission from the

Insurance Council of Australia

27 November 2017

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TERMS OF REFERENCE

That Portfolio Committee No. 4 – Legal Affairs inquire into and report on the funding of fire and emergency services, and in particular:

(a) the policy process and financial modelling underlying the provisions of the Fire and Emergency Services Levy Act 2017;

(b) the policy and financial implications for all stakeholders of repealing this Act;

(c) alternative models for ensuring that fire and emergency services are fully funded in a fair and equitable manner; and

(d) any other related matter.

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INSURANCE COUNCIL OF AUSTRALIA

1 Executive Summary

The economic case for the abolition of insurance-based taxes is widely accepted, having been canvassed in numerous Federal and State Government reviews and inquiries.

The Insurance Council and its members have long advocated for the abolition and replacement of the NSW insurance-based Emergency Services Levy (ESL) with an equitable property-based levy, consistent with all other mainland states. As such, the general insurance industry warmly welcomed the NSW Government's announcement in late 2015 for ESL reform.

Over the past two years, the Insurance Council and its members have committed considerable effort and resources in relation to ESL reform. This included working closely with NSW Treasury and the Emergency Services Levy Insurance Monitor (ESLIM) and his Office to achieve a smooth and harmonious transition to the new property-based Fire and Emergency Services Levy (FESL). The industry also offered to utilise the industry's data and expertise to assist Government model the rates for the new levy. However this offer of assistance was declined.

In view of the industry's full co-operation and compliance with the ESLIM's onerous regulatory requirements, the industry was disappointed it was not consulted on the NSW Government's decision in May this year to indefinitely defer the introduction of the FESL[1]. This deferral means that NSW continues to be the only mainland state that utilises insurance-based levies to fund emergency services, rather than replacing them with more efficient and equitable property-based levies.

Insurers have spent, and continue to spend significantly in terms of time, effort, and resources on systems changes, compliance, and communications to facilitate the removal and then re-establishment of ESL. Together with the inability to recoup the under-collection of ESL in 2015-16 and 2016-17, the failure to implement ESL reform has cost insurers over $40 million. This money has now been spent to no purpose. More importantly, the justifications for reform, vindicated by successful examples in other states, remain valid and we believe NSW is the poorer for them being put aside.

The Insurance Council strongly submits that the interests of NSW would be best served by proceeding with removal of the insurance-based ESL and its replacement with a re-modelled property-based levy, subject to safeguards as to its impact. The property-based levy remains the most economically effective, equitable and efficient method to fund the NSW Fire and Emergency Services (NSWFES). The property-based levy would be consistent with the user pays principle for government services; encourage the adequate use of insurance; and be a more efficient and certain way of collecting revenue compared to the unpredictability inherent to the ESL, which in essence, penalises policy holders for effectively managing their risks.

1 NSW Premier Media Release. May 2017.

If the NSW Government concludes that a property-based levy cannot be made to operate equitably, a number of alternative options remain which we believe would still be fairer to consumers and more easily administered than the ESL.

For example, funding for NSWFES could be sourced directly from NSW Consolidated Revenue recognising that the provision of fire and emergency services is a public good used by and for the benefit of the whole community. Alternatively, if the Government considers that the budget is unable to sustain new expenditure, NSWFES could be funded by replacing the insurance-based ESL with a fixed rate levy applied on policies currently liable for ESL. While not as economically efficient as the Insurance Council's preferred option, it would still have advantages in terms of simplicity, transparency and less costly administration processes over current arrangements.

2 Introduction

Three organisations in New South Wales (NSW) are responsible for the provision of fire and related emergency services: the Fire & Rescue NSW (FRNSW), the NSW Rural Fire Service (RFS) and the NSW State Emergency Service (SES), collectively referred to as NSW Fire and Emergency Services (NSWFES).

The expenditure budgets for FRNSW, the RFS and the SES are set each year by the NSW Treasurer using similar funding allocation methodologies. The majority of NSWFES funding (73.7 per cent) is provided by Emergency Services contributions required from general insurance companies. The balance comes from the NSW Government (14.6 per cent) and NSW local governments (11.7 per cent). The total amount of funding required for these services in 2017-18 is budgeted at $1.2 billion[2], with $793.75 million[3] to come from general insurers.

This in turn is collected via an Emergency Services Levy (ESL) on premiums for specified types of insurance policies, the key ones being contents, motor and commercial property. In setting levy rates, insurers must individually use best estimates of their market share in the previous year, the expected budget allocation for emergency services, likely developments in market growth for policy types, and commercial considerations. The likelihood of these uncertainties resulting in over or under-collections has been acknowledged by the Emergency Service Levy Insurance Monitor (ESLIM) [4].

NSW is the only main land state to fund emergency services through an insurance-based levy. All others have moved to more efficient and equitable funding through a property-based levy without major disruption.

The economic case for the abolition of insurance-based taxes and the impact their cost burden on the non and under insured is widely accepted, having been canvassed in many Federal and State Government reviews and inquiries including the Australian Government's Review of Australia's Future Tax System (or the Henry Tax Review), the NSW Independent Pricing & Regulatory Tribunal (IPART) Review into State Taxation, the Victorian Royal Commission into the 2009 Bushfires Royal Commission, NSW Government 2012 review *Funding our Emergency Services*, ACT Review of Taxation and numerous Productivity Commission reports. All have recommended the abolition of insurance statutory contributions to the fire services in favour of a broad-based tax.

Internationally, a number of models/approaches ARE used to fund the fire services although property-based systems and direct grants to the fire and emergency services are the most common form of funding. For example, the London Fire Brigade (an arm of the London Fire & Emergency Planning Authority) secures the bulk of its funding from central government

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2 Sum of 2017-18 budget allocations of FRNSW, RFS and SES, according to NSW Budget Estimates 2017-18 Paper No. 3, page 13.
3 The 2017-18 Insurer ESL Contribution target was based on insurers 2015-16 market shares, in accordance with the ESL Act to make for a normal year before the ESL reform. The Notice of 2017-18 ESL Contribution Target was published by NSW Treasurer in NSW Government Gazette No 80 of 14 July 2017, page 4101.
4 ESLIM's Guidelines on Price Exploitation, paragraph 64, page 18. July 2017.

funding and the remainder from London boroughs primarily though taxes on property[5]. In the United States, the most common taxes supporting fire and emergency services are property-based, levied at a set rate per dollar of assessed value[6].

5 London Fire Brigade, Statement of Accounts, 2007/08 and Victorian Department of Treasury & Finance (July 2003), A Review of Victorian Fire Services: Funding Arrangements, pages 104 – 105.
6 See US Federal Emergency Management Agency; US Fire Administration, Funding Alternatives for Emergency Medical & Fire Services. April 2012.

3 The policy process and financial modelling underlying the provisions of the Fire and Emergency Services Levy Act 2017

The general insurance industry welcomed the NSW Government's announcement in December 2015 that it would abolish the ESL and introduce a fairer property-based system of funding NSWFES. This reform had long been advocated by the Insurance Council and its members on the basis of equity and economic efficiency. In particular, it would help address NSW's high levels of under insurance[7].

In order to facilitate a smooth and efficient transition, the Insurance Council provided information to NSW Treasury on industry's experience with removal of Victoria's Fire Services Levy and similar reforms in other states and territories. The industry also offered to assist NSW Treasury with modelling the property-based Fire and Emergency Services Levy (FESL) but this was declined.

The Insurance Council was consulted in early 2016 on the draft bill to set up the regulatory regime around the Emergency Services Levy Insurance Monitor (ESLIM) which would govern the transition to a property-based levy. The Insurance Council and members also met with NSW Treasury on the (at that stage) proposed requirement for insurers to submit data via the ESLIM to assist with modelling the FESL. General insurers complied with the data requests but were not involved in any financial modelling.

On several occasions in early 2017, the Insurance Council met individually with Treasury and the ESLIM's Office to provide feedback on the *Fire and Emergency Services Levy Bill 2017*. In these discussions, the Insurance Council reiterated its members' offers of assistance in modelling the FESL.

The *Fire and Emergency Services Levy Bill 2017* actually instituting the move to funding through a property-based levy received royal assent in April 2017. However, at the urging of the NSW Government, the industry had been working for more than a year to ensure a smooth transition. On the basis of continued assurances that the reform was proceeding, in the months prior to the scheduled introduction of the FESL (1 July 2017), many insurers implemented a tapered reduction in ESL charges. This was principally to avoid public perceptions of double payment of emergency services contributions once FESL collection began and also to minimise compliance complexities that would have resulted from the need to return any over collections. However, the consequence was a significant under-collection of their emergency services funding liability for which insurers remained liable.

On 30 May 2017, the NSW Government announced that it would defer introduction of the FESL, and ESL would continue to be collected via insurance policies[8]. This was done without prior notification or industry consultation and with little regard to the industry's considerable efforts and expense to transition to the FESL and compliance

7 NSW Treasurer Media Release. December 2015.
8 NSW Premier Media Release. May 2017.

with the ESLIM's extensive requirements under the ESLIM Act. For example, for eight months insurers had been required to publicise and explain to their customers the impending reform, including through mandatory provision of a notice.

Following the announcement, the Insurance Council and individual members met with the NSW Treasurer, NSW Treasury and the ESLIM to discuss ESL re-introduction. After consulting with its members, the Insurance Council put forward suggestions to the NSW Treasurer on the best way of re-establishing ESL. However, none of the points advocated by the industry, such as prescribed ESL rates and a common date for insurers to restart ESL collection, were reflected in the ESL Act.

As well as deferring the FESL and continuing the ESL, the ESL Act provides a mechanism for re-activating ESL reform from 1 July 2019 through gazettal of a NSW Government notice before 1 July 2018. The Insurance Council and its members continue to advocate replacement of the current insurance-based ESL by a more equitable and efficient method of funding fire and emergency services.

4 The policy and financial implications for all stakeholders of repealing this Act

The NSW Government's decision to freeze the funding reform set out in the *Fire and Emergency Services Levy Act 2017* (the Act) means the continuation of an antiquated system of funding fire and emergency services through the insurance-based ESL.

The Government had promoted ESL reform as resulting in a fairer system under which all property owners, not just those with insurance, would contribute to funding the fire and emergency services and that this would place downward pressure on insurance premiums and help to reduce NSW's high rates of under insurance (see for example statements made by the current Premier when Treasurer)[9]. These justifications for reform, supported by numerous official reviews, reports, and successful examples in every other Australian mainland state, remain valid and NSW is the poorer for them being put aside.

Consumer detriment

After a major natural disaster in Australia, it is unfortunately common to hear of people who have lost their homes and possessions but are either uninsured or do not have adequate insurance to be able to properly recover from the losses they have suffered. According to data from the Australian Bureau of Statistics (ABS), it is estimated that of Australia's 8.4 million households which could potentially purchase contents insurance, 29 per cent (or 2.5 million) did not have a contents policy and of the 5.25 million potential buyers of home insurance, 3.8% do not have a building insurance policy[6].

A recent national survey undertaken by Understand Insurance, the Insurance Council's financial literacy initiative, found that more than 80 per cent of Australian homeowners and renters are under insured for their home and contents and 63 per cent of renters do not have contents insurance. While demand for insurance is influenced by various factors, such as demographics, dwelling type and tenure, the research indicates that insurance affordability is a key determinant of insurance take up[10].

The current ESL regime in NSW imposes a tax on people who protect their property, businesses and personal possessions by insuring them. The owners of non-insured properties make no direct contribution to the funding of NSWFES, while the owners of under insured properties pay less than the owners of fully insured properties when levies on the insurance industry are the main mechanism for funding NSWFES. This raises significant equity concerns and operates as a disincentive for property owners to purchase adequate insurance coverage.

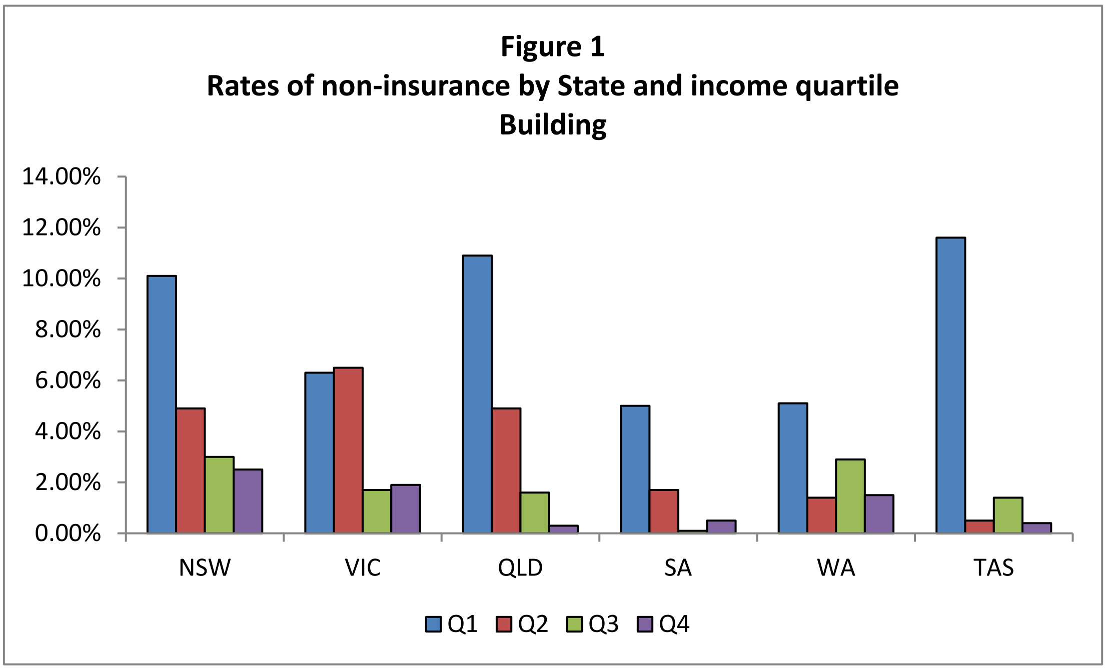
This disincentive is exacerbated by the combined effect of stamp duty and GST charged on insurance premiums, which distorts insurance price signals and reduces insurance affordability, increasing the risk that a household or business will under insure or not take out insurance. The layering of GST and stamp duty on top of an insurance-based ESL can lead

9 NSW Premier Media Release. December 2015.
10 Tooth, R. (prepared for the Insurance Council), Analysis of demand for home and contents insurance. August 2015.

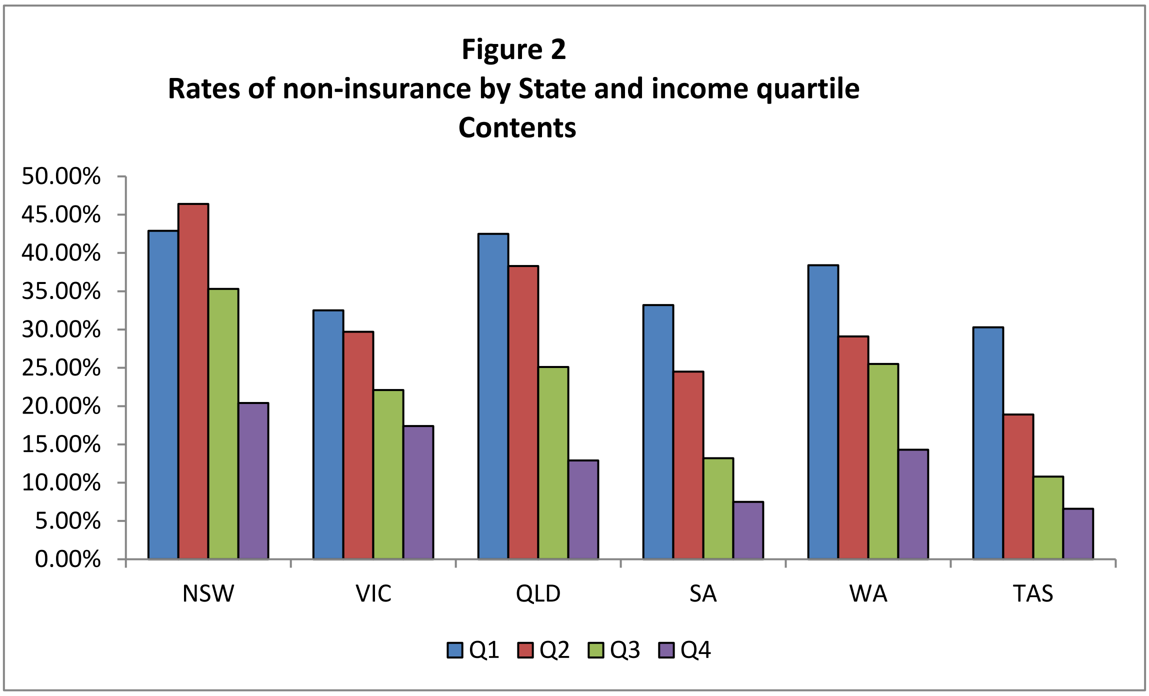
to effective taxes of around 45 per cent on a home insurance policy premium in NSW[11]. The effect of these charges often hit hardest on NSW small to medium businesses as commercial premiums are typically significantly higher than for consumer policies.

Research by the Insurance Council in 2015[12] examined the relationship between affordability and rates of non-insurance across states for building and contents insurance. This is illustrated in Figures 1 and 2 below. Figure 1 shows the rate of *building non-insurance* for owner occupied households that do not pay body corporate fees[13] by income quartile and state. Figure 2 shows the rate of *contents non-insurance* for all occupied households by income quartile and state.

In both cases, the research clearly shows that affordability and therefore the burden of taxation is a significant factor in determining a household's insurance status for lower income households, particularly for those in the first income quartile.



11 Insurance Council, Submission in Response to the Australian Government's Tax Paper. June 2015.
12 Insurance Council, Submission in Response to the Australian Government's Tax Paper. June 2015.
13 Households for which the decision to purchase insurance is a discretionary decision made by the owner whereas owner occupiers paying body corporate fees have building insurance purchased by the corporate body.



The Insurance Council's research[14] in 2015 also examined the impact of state taxes on the demand for building and contents insurance – both in terms of the decision to insure and the amount of insurance purchased – and estimated the changes if stamp duties (and the ESL in NSW) were removed from States and Territories. The research used ABS household expenditure surveys to analyse how expenditure on insurance varied with differences in tax rates between jurisdictions and over time.

The research estimated that the removal of all State taxes and charges would result in a $643 million (or 13 per cent) increase in the household's net (of tax) expenditure on insurance for their main residence (house or contents insurance)[15]. Over half of the increase (around 55 per cent) in total net expenditure is in NSW, reflecting that only insurance premiums in NSW are now subject to an ESL.

The removal of the ESL levy in NSW is estimated to increase net insurance expenditure by $226 million (or 16 per cent), and the removal of stamp duties in NSW would further stimulate spending by $125 million (or 9 per cent).

Importantly, the research also estimated that ESL removal in NSW would reduce the number of uninsured households, for house insurance, in NSW by 24 per cent, while the removal of

14 Conducted by Dr Richard Tooth of Sapere Research Group for the Insurance Council. This research updated demand elasticities initially estimated in 2008. The latest research incorporates data from the 2009/10 ABS Household Expenditure Survey, changes to tax rates and growth in the number of households since 2009/10.
15 There would be additional increases in expenditure on insurance for holiday and investment homes.

stamp duties in NSW would further reduce the number of uninsured households in NSW by an additional 10 per cent[16].

The Insurance Council's research also estimated that the removal of ESL and stamp duties in NSW would reduce the number of households without contents insurance by around 15 per cent. This cohort of uninsured households includes both owner occupiers and renters, the latter of which are estimated as being less responsive to a change in premiums arising from the removal of state taxes.

Impact on the NSW economy

NSW taxes insurance policies more heavily per capita than any other state in Australia[17]. The ABS data in Table 1 below demonstrates the substantial insurance taxation disparity between NSW and all other states in Australia in the 2015-16 financial year, when taxes on insurance in NSW totalled $2.44 billion.

Table 1

2015-16 Taxes on Insurance ($ million)

	NSW	VIC	QLD	ACT	WA	SA	TAS
Insurer contribution to fire brigades	**769**	0	0	0	0	0	17
Third party insurance taxes	212	185	0	0	0	48	14
Taxes on insurance not classified	1,456	967	41	44	615	414	69
Total taxes on insurance	**2,438**	1,151	41	44	615	462	100

The increased cost of insurance in NSW due to the ESL is also money that could be spent more productively elsewhere. In 2015, the Insurance Council commissioned research[18] to determine the economic impact of removing the ESL independently in NSW and also removing all insurance-based taxes in Australia, and in both cases replacing the insurance taxes with commensurate increases in municipal land rates (equivalent to a broad-based property levy).

Using computable general equilibrium modelling of the Australian economy[19], the research found that significant economic benefits could arise from removing insurance-based taxes and raising the revenue forgone through more efficient means. Specifically:

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16 This analysis was undertaken prior to the announcement of certain stamp duty exemptions for small business.
17 ABS, Taxation Revenue Australia. 2010-11, Cat.No. 5506.0, April 2017.
18 Insurance Council and Deloitte Access Economics. Impact of removing stamp duties on insurance. October 2015.
19 Comparative static computable general equilibrium model of the Australian economy with a representative household to model the impact of these changes on private consumption (as a proxy for welfare) and government budgets is recent best practice of modelling the impact of taxes in Australia, according to Cao, L. et al. Understanding the economy-wide efficiency and incidence of major Australian taxes. The Treasury, Australian Government. 2015; KPMG, CGE analysis of the Current Australian Tax System. Canberra. 2010; and Deloitte Access Economics, Analysis of state tax reform: Report for Insurance Council of Australia. 2011.

- Removing the ESL in NSW, and replacing it with commensurate increases in municipal land rates would lead to an increase in real consumption of 0.38% or $1.09 billion. Moving towards the more efficient tax base will increase economic activity resulting in higher tax receipts for government. This would mean that the removal of ESL in NSW would produce a net increase in NSW state and local government revenue of 0.30% or approximately $84 million.
- On a national level, the research determined that the removal of all insurance-based taxes across Australia, including the ESL in NSW, and replacing them with commensurate increases in municipal land rates, would lead to a net increase in real private consumption across Australia of $5.52 billion, and a net increase in tax revenue collected by state and local governments of 0.69%.

The impact of the ESL on non and under insurance ultimately increases the NSW Government's own financial exposure to catastrophic events through strong political pressure to meet community expectations of recovery assistance. It has been recently calculated that the total economic cost of natural disasters in New South Wales over the past decade averaged $3.2 billion per year and that the total economic cost of natural disasters in NSW will reach $10.6 billion a year by 2050, a growth rate of 3.4% per year[20].

The cost to the general insurance industry

The removal and then re-establishment of ESL has required NSW general insurers to spend significantly in terms of time, effort, and resources on systems changes and communications.

From information provided by thirteen of its members, the Insurance Council compiled the following estimates of the operational resources dedicated to the reform and reintroduction of the insurance-based ESL costs between early 2016 and November 2017:

- IT business and technical costs, including for development and testing:
  $11.6 million
- Compliance costs to meet ESLIM and NSW Treasury information and data requests:
  $1.4 million
- Customer communications costs:
  $1.4 million
- Human resources:
  105 Full Time Equivalent staff (FTE)

The sum of expenses attributable to ESL for this sample of insurers is substantial at $14.4 million. Furthermore, the opportunity cost of the 105 FTEs diverted from value-adding work must be recognised.

In addition, consideration must be given to the substantial losses insurers experienced due to the under-collection of the levy in 2016-17 (as explained on page 6). This under-collection was incurred while acting in good faith to allay public concern about double charging for

20 Australian Business Roundtable for Disaster Resilience and Safer Communities, Media Release. 21 November 2017.

emergency services funding. Based on figures from individual insurers, the Insurance Council estimates that the emergency services funding shortfall due to under-collection that industry needed to meet totalled approximately $30.1 million.

The significant costs to the industry from the removal and then re-establishment of the ESL come at a time when general insurers in Australia, and indeed around the globe, are facing significant pressures to manage volatility in their financial performance. It is critical that general insurers successfully manage this volatility and that the industry remains financially strong and stable, so that it can continue to meet its claims liabilities to policy holders.

In considering the money wasted due to the reversal of reform, it should also be noted that the Government assumed the $6.85 million cost of the ESL monitoring regime up until reform was delayed. Going forward, it is expected that this cost will be added to the emergency services contributions to be recouped from policyholders.

These substantial costs for industry and Government will be ongoing with the deferral of the FESL and exacerbated with any additional delay in reinitiating the ESL reform. As explained in the following section, the Insurance Council accordingly recommends the NSW Government reactivate ESL reform as soon as practicable.

5 Alternative models for ensuring that fire and emergency services are fully funded in a fair and equitable manner

The central issue with the insurance-based funding of fire and emergency services is that the "*majority of funding is provided by people who insure their properties, while people who do not insure their properties enjoy the same benefits"*[21]*.* The issue of free riders in the system was identified by NSW IPART as being a key reason why the horizontal equity (taxpayers with an equal ability to pay, pay the same amount of tax) of the insurance-based funding arrangement was particularly poor[22].

Fire and emergency services are defined as pure "public goods" to the extent that the use of the service by any one party does not (and should not) ration the availability of the service for another[23]. This fundamental characteristic of fire and emergency services lends itself to a funding model that seeks to share the burden of funding across the broader community in a fair and equitable manner.

As the NSWFES is public good utilised by the entire NSW community, the methodology used to collect its funding should observe the main principles of an effective tax. The effectiveness of a tax in achieving its purpose can be assessed against certain criteria, firstly by being equitable in terms of horizontal equity and vertical equity (meaning that taxpayers with greater ability to pay, pay more tax).

Furthermore, the effective tax should be:

- transparent and simple to understand;
- structured to minimise non-compliance; and
- ensure sufficient funds are reliably available to the government to enable it to adequately provide services expected by the community.

The current insurance-based ESL does not possess any of these characteristics. Nor does it uphold the effective tax criteria of efficiency, in that its imposition – as we have seen – raises premiums and as a consequence can affect consumers' choice to purchase insurance, creating a risk of under and noninsurance (as discussed in earlier sections).

Equitably modelled property-based levy

The Insurance Council strongly submits that the interests of NSW would be best served by proceeding with removal of the insurance-based ESL and its replacement with a re-modelled property-based levy subject to safeguards as to its impact. The property-based levy remains the most economically effective, equitable and efficient method to fund the NSWFES.

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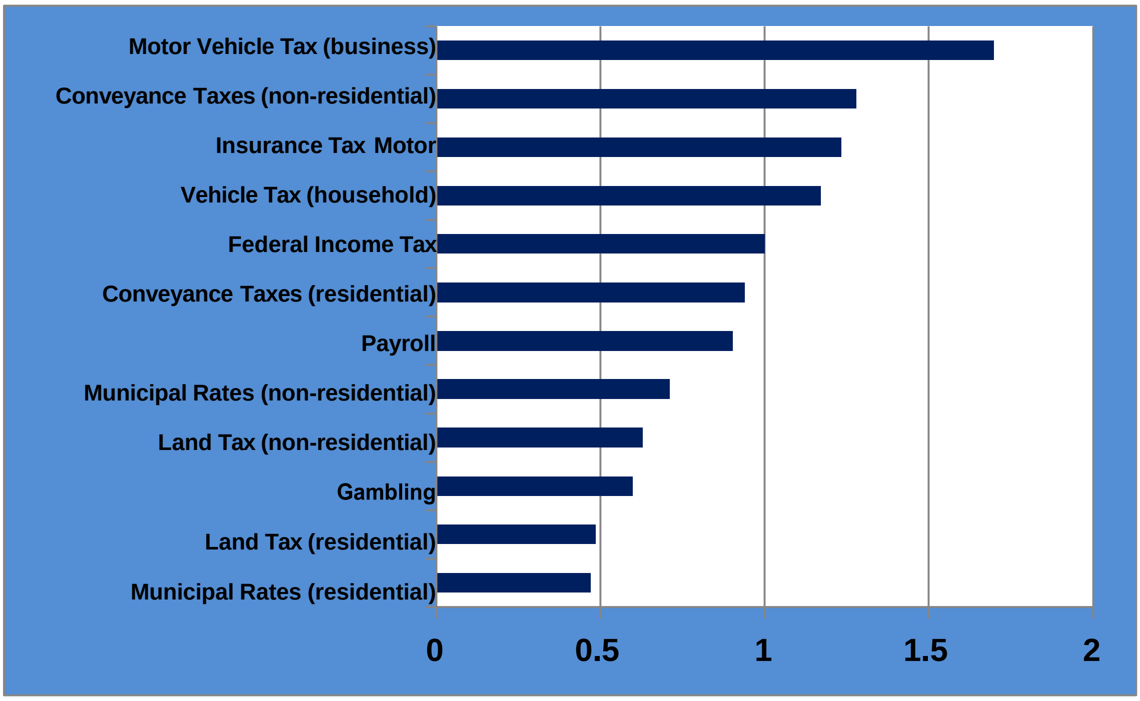
21 See NSW Government, Discussion Paper; Funding our Emergency Services, page 13. July 2012.
22 See NSW IPART, Review of State Taxation: Final Report to the Treasurer, page 69. October 2008.
23 A "public good" is described as a good where the use by one person does not reduce the consumption possibility for another. See Australia's Future Tax System, Report to the Treasurer: Part Two; Detailed Analysis, Volume 2: Glossary, page 743. December 2009.

Such a model would address the issues with the insurance-based ESL. It would be consistent with the criteria of an effective tax and the user pays principle for government services; encourage the adequate use of insurance; and be a more efficient and certain way of collecting revenue compared to the unpredictability endemic to the ESL.

In 2012, the Insurance Council conducted an analysis of the economic efficiency of the NSW insurance-based ESL and how the levy ranks in comparison to alternative State and local taxes[24]. The analysis demonstrates the economic welfare improvements arising from a switch away from an inefficient tax (such as the insurance-based ESL) to a more efficient State tax (such as municipal property-based rates/taxes)[25].

The taxes in Chart A[24] below are ranked in descending order from the least to the most efficient, relative to insurance taxes which has an index value of 1. It should be noted that municipal rates are not levied by State and Territory governments but were included in the analysis for comparative reasons because the State and Territory governments assumed responsibility for funding local government as part of the Inter-Governmental Agreement.

Chart A



This indicates that a broad-based municipal or land tax is highly efficient when compared to other possible sources of taxation revenue, including taxes on insurance. Indeed, the efficiency rankings highlight the scope for economic "upside" if NSW State

24 Analysis conducted by Deloitte Access Economics in conjunction with the Insurance Council for its submission to the NSW Government Discussion Paper Funding our Emergency Services. July 2012.
25 A municipal-based property tax is a proxy for a broad-based land tax wherein the base is unimproved land value and the tax includes in its base the principal place of residence.

and Local Governments were to shift their sources of taxation revenue away from transaction taxes (such as those on insurance and conveyancing) to taxes of a more immobile nature (such as land and payroll taxes) [26]. The abolition of insurance statutory contributions and the introduction of an equitable broad-based property levy would see the effective implementation of a key recommendation of the Henry Tax Review.

In addition to ranking NSW State taxes by their relative economic efficiency, the Insurance Council also examined the economic welfare benefit and the resultant economic efficiency "dividend" that would accrue from abolishing insurer fire levies with a broad-based property charge. This welfare analysis was undertaken under two scenarios, the first where only insurance contributions were replaced with a property-based charge, and the second where all statutory contributions were removed and replaced with a property-based charge[27].

The findings of the modelling are shown in the Table 2[28] below. The maximum welfare gain and revenue benefits arise from the transfer of all statutory contributions to a land based tax.

Table 2

	Welfare Increase*	Revenue Upside^
Insurer statutory contributions transferred	0.138%	$24.06 million
All statutory contributions transferred	0.187%	$33.16 million

Note:

* Welfare increase is the increase in household consumption

^ Revenue upside demonstrates the increase in Government revenue from changes in taxation bases due to taxation reform.

The NSW Government made the decision to defer the FESL in response to widespread reports from property owners that they were facing property levy rates significantly higher than the existing ESL and earlier FESL estimates[29]. For example, it was asserted by the Fire Brigades Employees' Union indicated that the FESL did not adequately reflect the relationship between contribution, risk and property value, used multiple unjustified base rates and did not distribute the cost appropriately between residential, commercial and rural properties[30].

26 This is consistent with the understanding in the Henry Tax Review and the IPART State Tax Review. The policy objective of shifting State taxes away from transaction style taxes to taxes on immobile bases was also discussed at the Commonwealth Taxation Forum in October 2011.
27 See Insurance Council submission to the NSW Government Discussion Paper: Funding our Emergency Services, page 8. 2012. The amounts modelled were as follows: the insurance component of $612 m (2010/11 dollars) and all statutory contributions of $912 m (2010/11 dollars). The results shown are for NSW only and assume the policy shift occurs in NSW only.
28 Source: Insurance Council of Australia and Deloitte Access Economics. 2012.
29 Source: Sydney Morning Herald, New NSW fire services levy delayed after furore. November 2017.
30 Source: Fire Brigades Employees' Union, Ten key problems with FESL. March 2017.

Given that these issues were successfully addressed by other states that transitioned away from insurance-based levies, the Insurance Council is confident that they can be overcome also in the NSW context. Lessons could perhaps be learned from other states. Although private land is the principal base for the emergency services levy, there remain significant differences in approach. For example:

- The method of calculation. In the case of Queensland, the levy incorporates stipulated risk factors depending on the activity carried out on the property. In Western Australia, the levy is a function of service levels with minimum payments and maximum caps in place and South Australia employs a land use factor for its emergency service calculation.
- The extent to which mobile property, such as for motor vehicles, is included in the levy net. In the case of South Australia, a fee is imposed on motor vehicles for purpose of emergency services funding.

Through its day to day exposure to risk analysis, pricing and underwriting operations, the general insurance industry is experienced in developing complex models which require high and exacting technical capabilities. The industry reaffirms its willingness to work with NSW Treasury to resolve the equity issues concerning the Government.

Alternative Funding Models

Despite a property-based levy being the best policy option for funding NSWFES, the Insurance Council acknowledges that the NSW Government has the responsibility to take decisions which it believes are in the overall best interests of the State's citizens. If the NSW Government concludes that a property-based levy cannot be made to operate equitably, then a number of other options remain which would still be fairer to consumers and more easily administered than an insurance-based levy. These options, expanded further below, include funding NSWFES either

- directly from NSW Consolidated Revenue; or
- by replacing the insurance-based ESL with a fixed rate levy

Consolidated Revenue

Funding for NSWFES could be sourced directly from NSW Consolidated Revenue; an appropriate method of funding a public good used by the whole community. Similar to a property-based levy model, this alternative approach would not discourage insurance use and would be a more efficient, certain and stable method of collecting revenue compared to an insurance-based levy.

The Insurance Council's research[31] in 2010 evaluated the impact of funding fire and emergency services under alternative options – such as through Consolidated Revenue – that extend beyond property-based system alternatives. The research estimated the impact of the modelled alternative options on economic welfare in Victoria, in terms of net improvement to welfare (being the net increase in household consumption in Victoria), and

31 Insurance Council, Submission to the Victorian Government Green Paper: Fire services and the non-insured. July 2010.

was conducted in the context of the removal of the then Victorian insurance-based Fire Services Levy.

The estimates of the research, presented in Table 3 below, showed that the introduction of a revenue-neutral municipal levy (essentially a broad-based property levy) would result in a 0.29 per cent net improvement to welfare in Victoria. The research found that the largest improvement to economic welfare in Victoria would be from implementing a grants based system funded from the Consolidated Fund (at a cost to revenue), which would result in a 0.94 per cent net improvement to welfare.

Table 3

Funding Model	Net Improvement to Welfare (%, VIC)
Introduction of a municipal levy (revenue neutral) [32]	0.29
A grants based system funded from the Consolidated Fund at a cost to revenue	0.94

Fixed rate levy

If the NSW government concludes that its budget could not sustain a new expenditure, NSWFES could be funded by replacing the insurance-based ESL with a fixed rate levy, similar to the existing stamp duty on insurance, applied on the policy types currently liable for ESL. While not as economically efficient as the options explored above, it would still have advantages over current arrangements.

A fixed rate levy would provide the NSW Government and NSWFES with the ability to determine and adjust rates, promoting predictability around funding allocation and budget forecasting. This would be a marked improvement on the uncertainty and complexity of insurers having to calculate individual rates on the basis of market expectations.

A fixed rate levy would also simplify compliance costs for the NSW Government and the industry. In a “normal” year, ESL collection costs general insurers tens of thousands of dollars each and the unwanted and unnecessary distraction for management of acting as a tax collection agent. On the Government side, there is the burden of maintaining a monitoring regime based on the ESLIM and having Revenue NSW deal with ESL as a separate revenue source.

32 The municipal levy is essentially the broad-based property levy as discussed earlier in this submission, see pages 13 and 17.

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