Mutual admiration

Businesses and groups battling insurance market problems may drive a renaissance in an alternative risk-sharing solution

By Wendy Pugh

Alpine lodges, Queensland churches, professional groups and amusement parks have all suffered insurance pain in the current market and all have discussed mutuals as a possible way out of their cover dilemmas.

After falling in and out of favour over decades in tandem with pricing cycles and capacity changes, mutuals are undergoing something of a renaissance as affordability and availability issues defy easy solutions.

"Mutuality has been on the back-burner in Australia for a while, but it has certainly been coming back to the forefront," Regis Mutual Management Director Gerald Ewing tells *Insurance News*. "There are significant challenges out there and that is driving a big increase in interest."

UK-based Regis Mutual helps create and manage mutuals. In Australia it is associated with Unimutual, formed in 1989 to assist universities and related higher-education and research organisations that had been struggling to gain cover. It also helped set up Perth motor trades insurance specialist Capricorn Mutual.

In the current tough conditions, described by Willis Towers Watson as the hardest market cycle since the mid 1980s, groups struggling with professional indemnity and liability cover are looking at mutuals, along with property holders in regions deemed exposed to cyclones and bushfires.

That includes lodges in alpine regions that have seen premiums skyrocket and capacity reduced since the Black Summer bushfires.

Mount Buller Ratepayers Association Director Chris Hollier says premiums for the Benalla Ski Club lodge have soared from $13,000 to $55,000 in two years. That's despite sprinkler systems, resilient building features and no history of bushfire losses on the mountain, as insurers take a sweeping approach to the risk.

"A more permanent solution, and to me a better one for the mountain, is a to have a permanent mutual in place, professionally run for the benefit of all participants and retaining the profits within it," he tells *Insurance News*. "Certainly, everybody who would be in it would have a mutual desire for it to succeed."

Preliminary explorations last year on a mutual-type arrangement didn't gain traction, but broader alpine options are being explored with insurtech Picnic Labs, which has an interest in mutuals in a variety of contexts.

However, there is a possible obstacle. Victorian alpine lease arrangements are held through resort management boards, which act as the Crown's representative. The boards require that buildings are insured, and mutual arrangements may not meet the criteria.

Operators of amusement rides, water parks and other leisure venues are facing similar stresses in public liability, with moves afoot to examine options.

The Australian Amusement Leisure and Recreation Association has entered into a partnership with Aon to look at the feasibility of an industry-owned discretionary mutual fund. It has already approached the Federal Government over a grant to get started.

The Australian Small Business and Family Enterprise Ombudsman is also looking at the proposal with the assistance of external expert advice.

Supporters of mutuals say they have lower costs, effectively assist groups with similar risks, retain profits and are better at driving mitigation. The concept harks back hundreds of years to the risk-sharing origins of insurance before shareholder-owned corporations became more dominant.

"One of the key differences in a mutual is that the customer and the owners are the same people," Mr Ewing says. "That removes one of the essential tensions you see in an insurance company – they do a good job of managing that tension, but it is always going to be there.

"Ultimately that is driving what we are seeing at the moment. In that need to return profits, they are having to push prices up and withdraw from certain areas because they are just not profitable enough."

Proponents of mutuals say their success in facilitating mitigation lies in the common nature of issues faced and a sharper sense of shared benefit from activities taken to reduce risk.

"A mutual is uniquely placed to address resilience and mitigation with its members," Mr Ewing says. "It is owned by its members, so they have a vested interest in its outcomes. But more than that it is because of the way a mutual communicates with its members."

Mutuals are structured in various ways and may include insurance mutuals regulated by the Australian Prudential Regulation Authority (APRA) and discretionary mutuals offering "insurance-like" protection products.

Motoring organisations that introduced insurance arms have a long history as mutuals, including RACQ in Queensland and RAC in Western Australia. In New South Wales, NRMA controversially demutualised its insurance business in 2000.

Discretionary mutuals aren't subject to the Insurance Contracts Act and have greater flexibility around accepting or rejecting claims. They don't have to meet APRA capital standards but are covered by Chapter Seven of the Corporations Act, which is regulated by the Australian Securities and Investments Commission.

Challenges starting a mutual include gaining sufficient initial capital and gathering commitments from sufficient potential members with similar risk profiles and values to justify the set-up processes.

Picnic Labs Chief Executive Charles Pollack says a 2019 legislative change allowing funds to be raised through mutual capital instruments (MCIs) has opened the way for a new generation of mutuals.

Australian Unity, operating in health and aged-care, became the first mutual to issue MCIs, raising $100 million in November.

Picnic launched the Our Ark mutual last year using MCIs, with the Anglican Diocese of North Queensland as a foundation member. The mutual is aimed at religious organisations, education, aged care, community groups and not for profits.

"We have been pleasantly surprised about the level of interest for members to join Our Ark," Mr Pollack tells *Insurance News*. "We had projections as you always do with a business plan, but I think it would be fair to

Deep trouble: finding insurance for ski lodges in areas like Victoria's Mount Buller is increasingly difficult

say the level of interest has exceeded the level we have allowed for in the projections."

In a submission to a Federal parliamentary committee inquiry, Picnic suggests change to regulations to allow MCIs to meet top-ranking Tier 1 capital requirements, facilitating mutual insurance product solutions in a wider range of areas.

Picnic Labs has also been looking at a consumer insurance mutual offering home, strata and other cover, especially to residents of northern Australia, but that type of arrangement would need to meet APRA capital requirements.

Picnic told the inquiry, which is examining mining and energy sector problems as banks and insurers withdraw support due to climate change issues, that regulatory changes could facilitate mutual solutions in the resources arena.

Mr Pollack was asked at an Actuaries Institute seminar whether MCIs, which can be redeemed or reduced as the mutual becomes self-sufficient, could lead to the types of issues faced by shareholder companies.

"That is an interesting philosophical discussion, when you establish the mutual," he said. "What are your plans for the MCIs; are the MCIs really there to be an initial float and ultimately as far as possible be removed from the capital base, or do you see them being in the long term a part of the capital base?"

Past demutualisations and stock market listings have been triggered by the lure of growth, a desire to raise more funds and members cashing in when changed market conditions mean mutuals are no longer seen as essential.

The current hard market is expected to prevail for some time yet, but there is a view that fundamental shifts may mean the attractiveness of long-term mutual arrangements goes beyond pricing issues.

"Our observation is that there are actually more systemic things at play," Mr Pollack says. "Irrespective of pricing cycles, there is a lot of relevance for mutuals in situations where there has just been a shift in attitude to the risk and the capacity has just disappeared or become very expensive."

The Australian Small Business and Family Enterprise Ombudsman has described current insurance affordability and accessibility issues as a national crisis, while the Federal Government has committed to a reinsurance pool with $10 billion in Government backing for cyclone and related flooding risks across northern Australia.

The Insurance Council of Australia has commissioned an independent review led by actuary and former APRA Member John Trowbridge to consider how the industry might respond. A consultation paper released last month includes mutuals as one of 16 options for feedback.

Sydney-based underwriting agency Asia Mideast Insurance and Reinsurance (AMIR), the Australian Financial Services Licence-holder for Our Ark and Aussie Farmers Mutual, earlier this year called for feedback on a professional indemnity pool, noting many businesses are being unfairly affected by a market over-reaction.

"If there are losses in professional indemnity, it is not for all professions," AMIR CEO Adel Dawood said. "You can't just treat everybody with the same brush."

Unimutual Acting Chief Executive and industry veteran Terry Ibbotson says setting up a mutual requires extensive historical data and analysis to understand the level of risk that should be accepted and how the mutual will operate. Establishment costs are significant.

"A mutual requires a longer-term commitment, and over the longer term it will definitely provide a more sustainable solution."

The long-running universities mutual follows APRA guidelines, even though as a discretionary mutual it doesn't come under the regime, and uses actuarial analysis to examine potential future losses and requirements.

"We retain the first $7.5 million of each and every loss on the property side and then we reinsure the excess of that amount in the traditional direct and reinsurance marketplaces both in Australia and around the world," Mr Ebbeson says.

Members will regularly test the market through their own brokers as part of procurement policies, while insurance companies may at times decide higher education is appealing and target the mutual's turf.

"It is not a protected animal," Mr Ebbeson says. "We have to fight every year and we have people in the field to make sure we have the most competitive product we can possibly have, with the broadest scope of cover, and we provide additional services for the members."

Mutuals that Regis has been involved with typically have retention rates of more than 90%, Mr Ewing says. Those that decide to become members tend to stay on board.

"If you are going to shop around all the time, then a mutual is not for you," he says. "A mutual requires a longer-term commitment, and over the longer term it will definitely provide a more sustainable solution and should produce cheaper pricing."

Concerns over value provided have been raised in the local government sector, where mutual arrangements have operated for decades, gaining traction in the early 1990s after insurance became almost impossible to buy.

Some councils in NSW and Victoria have argued better deals have been available at times elsewhere in the market, leading to class actions against JLT as manager and adviser and disputes over scheme deeds and the arrangement of protection.

JLT, now part of Marsh and McLennan, rejects the criticisms and says it services more than 300 councils across Australia through mutual schemes that provide stability and confidence to local government regardless of volatility in traditional insurance markets.

Internationally, mutuals have established a stronger general insurance presence in regions including the US and Europe.

One of the largest mutuals globally, Oil Insurance Ltd, began in the 1970s due to problems faced in the energy sector, while Mr Pollack noted at the Actuaries Institute conference that four of the top 10 insurers in the US are mutuals or reciprocal exchanges.

Mr Ewing says regulatory changes could be made that would reduce costs and improve the opportunities to form mutuals in Australia.

"Because discretionary mutual protection is regulated as a financial product, there is still a lot of red tape and compliance and governance required, and that is a barrier to entry," he says. "What we would like to see is a slightly lighter regime, particularly for the smaller groups, because at the moment it is smaller groups that are typically facing problems."

Proponents say that, in a sign of the times, more brokers are looking at the possibilities of mutuals as their clients struggle to gain cover, and that risk-sharing pools don't have to put intermediaries on the sidelines.

Mr Pollack says policyholders tend to lose out relative to shareholders when insurance companies over-react to perceived risks, imposing higher pricing and reduced capacity. "At the end of the day the customer is far from number one."

Currently, the greatest potential for expansion of the concept is through the discretionary model targeted at business needs, Mr Pollack says, although demand clearly exists also for solutions aimed at the more regulated consumer end of the market.

"Where there is capacity to be able to accept a product that is insurance-like rather than specifically being an insurance contract, there is huge opportunity."

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