31 July 2020

Mr David Thodey AO
Chair, Review Panel
NSW Review of Federal Financial Relations
NSW Treasury
52 Martin Place
SYDNEY NSW 2000

Dear Mr Thodey

REVIEW OF FEDERAL FINANCIAL RELATIONS – DRAFT REPORT

The Insurance Council of Australia[1] (**Insurance Council**) appreciates the opportunity to provide comments on the *Federal Financial Relations: Supporting the road to recovery Draft Report* (**the Draft Report**) released on 1 July 2020.

As explained in our earlier submission of 22 November 2019, the Insurance Council considers the Review of Federal Financial Relations (**the Review**) to be a significant and much needed opportunity for the NSW Government to evaluate its taxation arrangements. Action is necessary to ensure that as many impediments to economic growth as possible are removed and that revenue is sustainable into the future.

This is important if NSW is to continue to provide the high-quality services, such as emergency services, health and education on which the people of NSW depend. It is also important to ensure that revenue collection to fund Government services does not unnecessarily impinge upon the capacity of people in NSW to better their own lives and that of their families and communities through their own effort.

Since the Review was announced in August 2019, the scale of the damage wrought on individuals and communities, first by the Black Summer bushfires, and then by the ongoing COVID-19 induced recession, has only heightened the importance of resetting existing taxation arrangements so as to better respond to the needs of governments, communities and individuals. The Insurance Council considers the Review is an important part of that process.

[1] The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent about 95 per cent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system.

Insurance Council members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).

March 2020 Australian Prudential Regulation Authority statistics show that the general insurance industry generates gross written premium of $51 billion a year and has total assets of $133.8 billion. The industry employs about 60,000 people and on average pays out about $169.4 million in claims each working day.

Over the 12 months to March 2020 the industry's net profit after tax (NPAT) was $1.5 billion – a 56.7 per cent decrease from the prior year's NPAT of $3.5 billion. The industry's underwriting result was also $1.5 billion, falling by 47 per cent from $2.8 billion in the prior year.

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However, that process will only progress if there is the acceptance, at both a governmental and community level, that the current State taxation regimes and related Federal-State financial arrangements are no longer fit for purpose. The Insurance Council endorses the Review's statement that:

> "*A business as usual approach by our governments of today would create an inevitable legacy of undesirable choices for our governments tomorrow"* [2].

We therefore welcome the pragmatic approach taken in the Draft Report. It recognises that while a whole of government (Federal, State and Local) approach, consistent with a vibrant federalism, is needed in respect of some of the mooted reforms (most notably the GST), this should not delay State governments from progressing reform where they can:

> *"No government has the option to sit back and do nothing"* [3].

The Insurance Council is very much of the view that in relation to taxation reform, perfection should not be the enemy of the good, particularly when all stakeholders agree that the current situation is less than good.

As recognised in the Draft Report, taxes on insurance have been consistently acknowledged by a long series of inquiries to be inefficient, inequitable, regressive and administratively burdensome. The Insurance Council therefore welcomes the strong recommendations in the Draft Report and completely agree that:

> *"There is no principled case for applying a special tax on insurance*" [4].

This finding and the views expressed in Chapter 6 of the Draft Report are consistent with the well-established policy and empirical evidence referred to in Chapter 6 and in the Insurance Council's submission of 22 November 2019.

The Insurance Council supports the draft recommendations in the Draft Report that:

- *"All specific taxes on insurance products, including the Emergency Services Levy in New South Wales, **should be abolished** and **replaced by more efficient and broad tax bases**, to improve the affordability and uptake of insurance.*

- *To reduce the cost of insurance and enable fairer ways to fund the fire and emergency services, the Government **should reconsider applying a levy on property owners** and should also consider combining this with any future broad-based land tax. The reform should follow a detailed consideration and modelling process to carefully consider the impacts on different taxpayers." (**emphasis added**)*

The consequences of the blunt application of taxes on insurance - their unfairness, their inefficiency, their regressive nature which leaves low-income households more exposed to loss in adverse circumstances, are all noted in the Draft Report. Given this, there is no apparent reason why these recommendations are not at least as strong as the Draft Report's recommendation in relation to transfer duties on real property:

[2] Page 7, the Draft Report
[3] Page 8, the Draft Report
[4] Page 85, the Draft Report

> *"A more equitable and efficient approach to taxation, the NSW Government* ***should replace duty with a broad-based land tax.*** *The transition should be managed with the support of detailed distribution and financial modelling and public communication and consultation, so that the transition is fair, efficient and minimises the amount of revenue foregone*[5]*."* (***emphasis added***)

Given the universally acknowledged harmful impact of taxes on insurance we would have thought an equally strong final recommendation for their replacement was merited.

The Insurance Council submits that the Review's initial finding that:

> *"A broad-based land tax is the best instrument for this task, and a transfer duty to land tax switch would establish the right settings for fiscal recovery and long-term growth*[6]."

equally applies to stamp duties on insurance and the emergency services levy.

With the Australian economy needing to regain momentum after being hit by COVID-19, Australian Governments at all levels need to take account of the economic impact of removing stamp duties and other levies from the cost of insurance. As noted in the Insurance Council's submission to your review, research has found that the removal of all insurance-based taxes in all states and territories and replacing them with commensurate increases in municipal land rates/property taxes 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, territory and local government of $575 million after five years if this reform were implemented Australia-wide. [7]

This is additional money that could be put to many good uses by Government.

If you have any questions or comments in relation to our submission please contact John Anning, the Insurance Council's General Manager Policy, Regulation Directorate, on telephone: 02 9253 5121 or email: janning@insurancecouncil.com.au.

Yours sincerely

Robert Whelan
Executive Director & CEO

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[5] Page 49, the Draft Report.
[6] Page 43, the Draft Report.
[7] 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.