

Flood Cover, The Insurance Ombudsman Service Perspective

The IOS Panel has dealt with probably 500 flood-related disputes. Some of the locations include Benalla Vic, Coffs Harbour NSW, Townsville Qld, Katherine NT, the Buckland Valley Vic, Wollongong NSW, Cape York Peninsula Qld, coastal locations north of Perth in WA and Brisbane. Many sections of the industry were initially reluctant for the Service to deal with these disputes claiming that disputes of this nature were not appropriate for an alternative dispute resolution process and should be determined by the courts. However, in my opinion, by dealing with them in the manner in which we have, we have introduced speedy, cheap and effective dispute resolution, certainty, legal accuracy and by skilful use of our inquisitorial powers, an ability to investigate these disputes with more flexibility than the court-based adversarial system.

It is trite to state a flood devastates a community physically. However, flood disputation can devastate a community physically and financially and there are numerous factors that have emerged in the 14 years since we commenced doing that work, that have not always shown the key players in a favourable light. In that regard, I refer to State governments, local councils and the insurance industry. The principal factors that have contributed to this situation are as follows:

1. The varying attitudes of insurance companies to flood related disputes. In my experience, some companies will pay the claims irrespective of the policy terms. Others will strictly apply the exclusions to cover, whilst others have initially denied claims and then reviewed their attitude, sometimes following media or community pressure. There is nothing that can divide a community more when the owners of household numbers 4, 6, 8, 10 have their claims paid and the owners of household numbers 3, 5, 7, 9 have their claims denied or when home contents insurer has accepted the claim, and the buildings insurer has denied the claim.
2. The attitudes of various councils has also been significant. When we were investigating the claims at Katherine and Townsville, the council representatives could not have been more helpful in assisting our understanding of the topography, the stormwater drainage systems and steps taken in relation to flood minimization. However the councils associated with the Wollongong floods in 1998, were circumspect and unhelpful as they were concerned they might themselves be involved in litigation.
3. It has been very interesting as I have travelled around Australia, inspecting many flood sites, to observe where residents have been permitted to build. This was particularly relevant in the Wollongong area where we observed homes built next door to strong-flowing creeks or over drains, formerly creeks, or on the edge of cliffs. As we inspected one property which had partially collapsed due to earth subsidence, we heard the sounds of building recommencing at a neighbouring property which was in an equally precarious position. It seemed as if the council's planning authorities had not learnt from the experience (nor for that matter, the owners).
4. I observed during a tour of Northern New South Wales in the Coffs Harbour region, how many people built their homes on flood plains. There was a resignation in some people when their houses were flooded that this was simply a price they paid in return for their chosen lifestyle. Wollongong had been the subject of 15 or more episodes of flooding over the previous 50 years, so those residents knew what to expect in some areas, but in others built in apparently safer regions, the shock and devastation was entirely unexpected e.g. due to blockages in creeks forcing water to higher regions. In 1999, the floods we investigated in Katherine, Townsville and Wollongong were one in 100 year events.
5. It was also quite fascinating to observe the different attitudes of the various communities in respect to flood damage. People in Wollongong were very active and they were supported by community groups, competent activist lawyers and the irredoubtable *Illawarra Mercury* who provided lists of insurance companies who paid claims and lists of insurance companies who denied them. A

demonstration outside the home of a CEO of one major insurance company, who lived in the general area resulted in a massive change of attitude on the part of that company. However, the people of Katherine were more passive as they, in general terms, belonged to a different socioeconomic group and believed insurance companies were too monolithic and impenetrable to challenge and when their claims were denied, they stayed denied. There was however a group of activists who did their best to motivate people to challenge the insurer's decisions.

Definitional Issues & Standardisation of Terminology

There are as many definitions of "flood" as there are roulette systems. Usually a flood is where water escapes from the confines of a natural watercourse, creek, storm, river, lagoon or lake. However, many definitions introduce additional concepts such as an artificial or modified watercourse which might include a drain, even one constructed in an area which had not previously been a watercourse.

Sometimes the term "floodwater" also included water that was rainwater but which could not escape from the area in which it fell because of the existence of floodwater, so that if a body of water then mixed with the floodwater and flooded the property, the damage was excluded.

Sometimes it was necessary to prove the watercourse had "banks", from which the water escaped, which was difficult if the alleged watercourse was no more than a indentation or a trough through which water intermittently flowed.

Sometimes water which flowed back through sewerage pipes and into the home, was excluded because it could not escape through the presence of floodwater, was deemed to be floodwater by the policy.

In terms of communicating the policy terms, many of you may be aware that standard cover as contained in the regulations made pursuant to the Insurance Contracts Act includes flood cover (see regulation 10). In these circumstances, it was important to consider whether the flood exclusion was clearly conveyed to the policyholder, because if it was not, the standard cover prevailed so that, contrary to the insurer's intent, the flood damage was covered. In one policy, we found the flood exclusion buried under the definition of "home buildings" at page 20 of the policy. I conducted a competition amongst IOS decision-makers to see how long it took to find the exclusion. One of my more experienced colleagues found it in 15 minutes. I came last as it took me 27 minutes to find it. Sam Parrino wondered if I could have perhaps employed my time more profitably.

We discovered in Katherine that the TIO (one of the last government insurance offices) provided a policy that included flood cover, however, the major competitor which was privately owned, marketed a policy that excluded flood cover. A number of policyholders complained that, in the last renewal before the January 1998 flood, their brokers, bank managers and other professionals persuaded them to change from the TIO to the other insurer on the basis the policy with the latter insurer was more advantageous. This was also a source of litigation.

The point therefore that must be made is there needs to be a more unified approach by the industry to this problem. As our beloved Prime Minister keeps telling us, one day the drought will be over and floods will again be a part of our lives. We have had a tremendous opportunity to learn from the great floods of 1998 and beyond, but I am not sure we have as yet done so. At a recent conference I attended on this issue, I discovered from many representatives of the industry, there remain many different approaches to this subject and I list but a selection of them.

- Some companies will not provide flood cover at all.
- Others will do so for a price or based on location e.g. they will cover the hippy commune at Mt Toolybewong.
- Others will cover flash flood whatever that means but not ordinary flood.
- Others will cover it similar to TIO.

The Insurance Council was at one time working hard to achieve standardisation in the industry as to the definition of "flood". They appear to have had some success in that regard.

I must say one of the major impacts of our decision-making has been to create the impression we will pay everything and there is no point denying a flood-related claim unless there is overwhelming evidence of floodwater damaging the property. This has meant a significant reduction in flood-related disputation. However, I am sure the drought we are experiencing in that process will break at the same time as the meteorological drought passes.

Consumer Attitude towards Flood Cover

As I said, many people who have built on flood plains, (mostly at Coffs Harbour) or near rivers and creeks (Wollongong and a great deal of northern New South Wales and southern Queensland), fatalistically accept that flood is a part of life but the majority of consumers desperately want protection against such a catastrophic event. I have observed some people almost suicidal after having experienced a terrifying flood event, to have observed the damage, and the aftermath, and then to be told contrary to expectation, the policy does not provide cover (and in some instances, to observe their next-door neighbour has had their claim paid). Such a scenario is likely to produce a public relations disaster for the insurance industry perhaps more than any other insurance-related event.

Until these issues were publicised, the majority of insureds believed they did have flood cover because, as we all know, nobody reads an insurance policy which is as impenetrable and difficult to read as *Ulysses* or *In Remembrance Of Things Past*. Now many people, particularly in areas which are subject to regular flooding such as Wollongong, Coffs Harbour and Katherine, are more vigilant in this regard, and are making demands on governments, local councils and their insurance companies to address these issues.

Progress and Development

In discussing progress and development, I think it is important to outline what happens in a flood-related dispute at IOS. Initially we receive written submissions from both parties. The dispute will usually centre around whether the damage to the property has been caused by stormwater/rainwater or floodwater. A typical scenario is that, following heavy rain, water has pooled around the property to an extent where the policyholder believes it has entered the property to a depth of six to twelve inches, and at some time later, floodwater enters the property from a nearby creek. If these facts can be established, and the onus is on the insurance company to prove the exclusion, the policyholder will be successful to the extent the insurance company will be ordered to pay for the stormwater damage which usually encompasses carpets, furniture, ornaments etc.

However, in many instances, it is not as simple as that and frequently a passionate dispute will arise as to whether, in view of the size of the local catchment area, it was possible for the rainwater to enter the property or whether the water from the creek reached the property first. Pursuant to case law, if a mixture of stormwater and rainwater causes the damage, the excluded event prevails over the included event so the flood exclusion defeats the claim. The problem of making factual findings is usually exacerbated by the fact the policyholder is not present, or the property may be tenanted so a degree of factual reconstruction is necessary.

This is where the experts, the hydrologists, become important, as they profess to have expertise based on information provided by councils and emergency services in determining the flow of the water in relation to the topographical features of the property. Unfortunately, they suffer from the same shortcomings as racehorse and football tipsters as they frequently disagree. We had to deal with one case in Brisbane three years ago where, on conducting an inspection of the property, each party's

hydrologist was adamant, in terms of a fence that had been flattened, that it proved the theory advocated as to the direction from which the water came in supporting their differing opinions.

These cases represent some of the most difficult fact-finding work the Panel is required to do, which makes it imperative progress and development in this area occurs so as to minimise disputation, and create a much more predictable basis for resolution of disputes. At the present time this issue has the potential to damage the reputation of the insurance industry, and other stakeholders and we have all been spared further consideration of this issue by the impact of the drought and that the number of flood-related disputes have diminished as a result.

From my perspective, the following needs to occur:

- Whilst I understand the spirit of competition is a driving force within the industry, issues relating to climate change, particularly concerning the problem of flood, need to result in a greater standardisation of policy terms, in terms of the cover provided in all the areas where people are permitted to build in vulnerable areas.
- Greater co-operation between councils, shires, all levels of government and the industry needs to occur. In my opinion, particularly in areas such as Wollongong and Coffs Harbour, many houses should not have been built so close to an area which had the potential for flooding. This in turn has led to local authorities being reluctant to be involved in providing information and/or in co-operating in allowing a level of understanding of the issues in dispute, and later in dealing with the reasons for minimising future problems of this nature. The insurance industry has blamed local authorities for their failure to share information in these areas, and has perhaps used the failure of other persons to robustly deal with these problems, as an excuse for not being sufficiently proactive themselves. Of course, some local authorities are much more willing to address this problem than others.
- From my many and varied travels, I have learnt the great majority of people expect insurance companies to pay for water damage, irrespective as to how it occurs. People were generally shocked to be told the damage to their properties was not covered, which represented yet a further blow. Their shock was transformed into rage when they heard that neighbours and other property-owners nearby were, for one reason or another, covered for the same event. If an insurance company does not want to cover flood, then it is important the documentation it produces not only clearly conveys such an exclusion, but that it is highlighted prominently early in the policy.
- I would like to see a meeting between all stakeholders to discuss these issue involving participants at federal state and regional levels as well as the industry. I predict the lull in flood-related claims will end sooner rather than later, and in my opinion, the problems raised at this conference require dynamic and aggressive attention.
- In the event the level of disputation in this area remains high, it is crucial the public have available to them, an effective and speedy means of dispute resolution. In this regard, I make the comment that a small number of cases did proceed into the formal court system and they took literally years to resolve, at least one I know, after an appeal to the Full Court of the Supreme Court. In my opinion the adversarial court system is not as effective in dealing with large numbers of these disputes, because it is essential to actually inspect the site and surrounding areas to understand the topographical aspects of the dispute, because no diagram, map or photograph can adequately depict these matters. A speedy resolution to these disputes has, in my opinion, saved many people added misery from the costs, delays and uncertainties of being involved in the adversarial process.

I hope that my unique perspective on these issues has been valuable.