Senate Finance and Public Administration Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE
SUPPLEMENTARY BUDGET ESTIMATES 2012-2013

Finance and Deregulation Portfolio

Department/Agency: Department of Finance and Deregulation
Outcome/Program: 2/2.3
Topic: Funding for NDRRA

Senator: Xenophon
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Question:

a) Is it true that with the exception of some insurance taken out by the state of Queensland for non-road assets, the Federal Government continues to be exposed to the same level of possible funding under the revised NDRRA for State and Territory disaster, than before the NDRRA amendments were made in March 2011? I set out below a table from Appendix 1 of the Review of the Insurance Arrangements of States and Territories under the Natural Disaster Relief and Recovery Arrangements (NDRRA) Determination 2011 (Phase Two Report).

Figure 1: Insurance Arrangements of States and Territories

	ACT	NSW	NT	QLD	SA	TAS	VIC	WA
Non-roads	✓	✓	✗	✓	✓	✗[1]	✓	✓
Roads	✓	✗	✗	✗	✗	✗	✓	✗
Terrorism[2]	✗	✓	✗	✓	✗	✗	✗	✓

[1] TAS has insurance arrangements in place for the Tasmanian Museum and Art Gallery collections for losses in excess of $5m and for marine hull assets up to $10m.
[2] Although not specifically referenced in the Determination, the then Attorney-General announced terrorism as an eligible event on 2 July 2010.

b) You say in the Review of the Insurance Arrangements of States and Territories under the Natural Disaster Relief and Recovery Arrangements (NDRRA) Determination 2011 (Phase Two Report), and I quote *"that investigations into the availability of commercial insurance for road assets and non-traditional insurance options for the transfer of risk identified that the appetite and capacity for these to be insufficient and even if available, may not be cost-effective"*. Please explain your findings?

c) Did your investigation include global reinsurance offerings (or did you just speak to Australian reinsurers), catastrophic bonds, parametric insurance or even a national pool scheme for road assets as possible solutions?

d) Even for the states which do have some insurance for non-road assets, such as SA, NSW, VIC, ACT, WA & to some extent QLD while you have said that you believe they may not be appropriate you have nevertheless not made any firm recommendations as to their appropriateness in accordance with the obligations under the Determination and the subsequent review of thresholds for assistance. What is required to do this and when do you think it will be completed?

Answer:

a) Yes.

b) The transfer of risk in respect of road assets is a very complex matter. Finance's findings on road insurance are detailed in Chapter 7 of the *Review of the Insurance Arrangements of State and Territory Governments under the Natural Disaster Relief and Recovery Arrangements Determination 2011- Phase 2 Report* (the report). The following extracts from the report (page 39) provide Finance's general observations and explanations regarding risk transfer options for road assets:

The appetite and capacity of traditional insurance arrangements for road assets in Australia is insufficient.

Traditional insurance products have proven difficult or impossible for some jurisdictions to access. There is currently limited capacity available in the market, and limited appetite for the cover given the poor loss experience in some geographic regions. In addition, the limited data held by some jurisdictions, particularly with respect to claims history, contributes to the limited interest by insurers.

Non-traditional insurance options are limited in their availability and, even if available, may not be cost-effective.

Non-traditional risk transfer options offer quick access to capital following a disaster. However, they are very risky. Capacity in the market is very tight. Market participants advise an upper limit of around $250m. The level of cover that could be purchased may make little difference in the event of a major disaster relative to its cost. These options can be expensive, although actual pricing is difficult to gauge given the tailored nature of the products. A parametric solution for road assets may not be a viable solution for reducing States' exposure in all cases.

Risk transfer options for road infrastructure may not present a viable solution for all jurisdictions in Australia.

It is evident that risk transfer options do exist—with the right data, the right product, and the right structure at the right price. However, the limitations of these options indicate that risk transfer for road assets, whether traditional or non-traditional, may not be a viable solution for most jurisdictions.

c) Chapter 7 of the report details Finance's investigations into non-traditional risk transfer options (including parametric solutions and catastrophe bonds) and alternative funding options including a national roads pool and concessional loans. Consultation was undertaken with Australian and global reinsurers. A full list of the parties consulted is at Appendix B of the report.

d) The appropriateness of insurance arrangements for states and territories (States) was assessed against a qualitative benchmark that reflects the obligation on States to identify their risk exposures and make fully informed decisions with respect to financing potential losses. Recommendations 3 and 4 in the report address the need for the Northern Territory and Tasmania to adopt the qualitative benchmark process and submit a further independent assessment to the Commonwealth for review. Whether the recommendations in the report will be implemented is a decision for the Attorney-General in accordance with Guideline 5/2011 of the NDRRA Determination. As stated in the report, Finance will further consider recommendations as to differential thresholds or differential rates of assistance for these States depending on the adequacy of the States' responses, subject to recommendations 3 and 4 being accepted. The report also includes several findings (Findings 2, 3, 4 and 5) with respect to differential thresholds that reflect the need to ensure that Commonwealth assistance is structured in a way that best incentivises States to engage in risk management and mitigation activity rather than set an arbitrary threshold for compliance.