



Mind the gap

Australia's terrorism reinsurance pool still excludes cyber, leaving the nation potentially exposed

By John Deex

Next month the Australian Reinsurance Pool Corporation (ARPC) will publish a major piece of research on cyber terrorism.

Developed in conjunction with the Organisation for Economic Cooperation and Development (OECD) and the University of Cambridge's Centre for Risk Studies at the Judge Business School, the study aims to identify current and prospective threats.

It also explores the practicalities of extending insurance coverage in Australia to include cyber terrorism – because currently the ARPC scheme wouldn't respond.

The way the scheme works today is relatively simple. Following the events of September 11, 2001, commercial insurers in Australia and around the world introduced terrorism exclusions.

But, under Australia's Terrorism Insurance Act 2003, when a terrorism event is declared these exclusions are removed and insurers must pay the claims.

Insurers can self-insure for this eventuality, arrange their own reinsurance, or

transfer their liability to the ARPC scheme. The vast majority – about 99% – use the ARPC.

The scheme covers biological and chemical terror attacks, but – in line with global industry practice – not nuclear. And, currently, not cyber either.

"If there was a cyber terrorism incident, we have an exclusion in our scheme for computer crime which we believe would exclude the cover," ARPC Chief Executive Christopher Wallace tells *Insurance News*.

"An example would be a building control system that has been interfered with, which causes a fire, and the fire damages the building. In that scenario the cause of the loss is computer crime, which would result in the scheme not responding."

Other schemes around the world do include cyber cover, and the ARPC has consistently flagged the potential gap.

But the most recent review by the Federal Treasury, carried out every three years, declined to expand the scheme.

"Treasury looked at this issue as part

of the 2018 review and recommended that more time was needed to understand whether the market would develop to cover the risk," Dr Wallace says.

"We've been doing some research on what the possible scenarios are, how big losses could be, and how are they covered in insurance policies.

"Many of the cyber policies that are emerging in the market do provide a small amount of cover for physical damage but often it has a very small sub-limit.

"That means there is only a very small percentage of cover available for those large commercial assets."

ARPC is hosting a cyber terrorism stakeholder seminar on March 18 at NSW Parliament House, and the study's findings will be published at this event.

Dr Wallace hopes the research will ensure that the issue is considered again.

"I'm hoping that the research we have done on cyber terrorism will help inform the next triennial review, so we can look again at how insurance policies are



developing, and how this risk is being covered internationally.

“It’s a real issue for business. We need to modernise the scheme to reflect the current risk environment and the way policies currently operate in the market.”

The cyber research is not the only major piece of work ARPC has undertaken recently.

It’s working with Standards Australia to develop a handbook for business on physical protective security for buildings. The handbook covers malicious attacks, criminal attacks, and also terrorism. It’s at an advanced stage and should be published in draft early next year.

“It will be the first in the world in terms of a codified set of guidelines around risk mitigation for malicious physical attacks.”

Dr Wallace was recently appointed President of the International Forum for Terrorism Risk (Re)Insurance Pools. It’s a role that will provide increased insights into similar schemes and industry challenges across the globe.

As the forum’s President, Dr Wallace will

**RYNO
INSURANCE**
UNDERWRITING

Tailored solutions for

- **Blue Collar**
- **Hospitality**
- **Property Owners**



Blue Collar | Hospitality | Property Owners

Call **1300 650 670**, visit rynouw.com.au
or email hello@rynouw.com.au

Ryno Underwriting is a division of East West Insurance Brokers ABN 83 010 630 092, Australian Financial Services License No. 230041. Ryno Underwriting acts under a binding authority agreement on behalf of certain Underwriters at Lloyd's. Refer to the Product Disclosure Statement or Policy Wording or call us on 1300 650 670.



Pushing for cyber cover: ARPC's Christopher Wallace

“The most likely attack is an unsophisticated attack causing injury or harm. But a large, complex asset-based event is still a possibility.”

take a leading role in preparing for the annual conference, set for June 3 in Washington DC.

“ARPC already participates in the forum and it’s a real privilege to be asked to chair it,” he says.

“There are many issues around the nature of the risk that are quite global, including use of drones, biochemical risks, defining war, terror and crime. There is a lack of clear definitions internationally around the difference between war, terrorism and crime.

“In the cyber space, we are seeing a trend emerging of hybrid attacks where it is unclear whether it is a nation state, or a criminal group, or a terrorist group. There is work going on at the moment trying to clarify the definitions at an international level.”

ARPC is a world leader in modelling, and regularly revisits what a maximum loss event in Australia could look like.

“We are confident that we can cover two significant loss events, which we think is adequate,” Dr Wallace says.

“Nuclear and radiological has always been excluded from our scheme. Most policies exclude it straight up, anyway. If there was an event of that magnitude it would be society-changing, and the community would have to decide at the time how it might respond.”

ARPC keeps a close eye on the evolving terrorist threat, from which Australia is far from immune.

Since 2014 there have been seven terrorism incidents in this country, with one declared for the purposes of the legislation governing the scheme. There have been 17

attacks foiled during the same period.

“We get a daily feed from public sources and we do connect with government on the risk as well,” Dr Wallace says.

“There is a lot of mitigation going on to keep the community safe, and the risk is real.

“The most likely attack is an unsophisticated attack causing injury or harm. But a large, complex asset-based event is still a possibility.

“If you look at the long-term global experience you do see big events over 10-15 year cycles. They can be anywhere in the world, and Australia is not immune from that.

“I’m very grateful that we have not had a significant event. It is good for us as a community and I hope that we don’t ever have to confront that.

“But it could happen.” □

Necessary backstop

The ARPC was never intended to be a permanent solution, but there’s no doubt that its role remains a crucial one.

Under Dr Wallace’s leadership the scheme remains strong, with net assets of \$461 million, a retrocession reinsurance program, and also the Commonwealth Guarantee.

Added together these give the ability to fund up to \$13.6 billion of losses.

“The Terrorism Insurance Act specifies in the legislation that an insurer that is insuring with ARPC transfers their full liability to us above their deductible,” Dr Wallace says.

“For insurers it is a very strong financial support. There is complete certainty in terms of

that transfer of risk. We wrote \$204 million in premium income last year, with more than 220 ceding insurers in the pool.”

ARPC’s retrocession program is in the process of being renewed, and it hopes to reduce its deductible and increase coverage by \$100 million.

“That will mean that the reinsurance program which is being placed back into the private market will provide capacity of \$3.45 billion as part of our whole funding ability.”

Dr Wallace says the last Treasury review, plus a performance audit by the Australian National Audit Office, have shown ARPC to be “efficient and effective” and also necessary.

“[Treasury] spent quite a bit of time talking to stakeholders. That review confirmed that there was a need for the scheme to continue,” he says.

“Insurers and reinsurers provided feedback that if the scheme didn’t exist then [the potential for] market failure would be exacerbated. The report shows really strong stakeholder support for what the scheme is trying to do.

“These two external reviews have been very thorough, and shown us to be in a strong position. I’m very proud of the ARPC team for the outcomes that the organisation has achieved.”