ARPC

Australian Reinsurance Pool Corporation

Annual Report 2006-07

ISBN 0 642 74407 6

A copy of this document appears on the Australian Reinsurance Pool Corporation website (www.arpc.gov.au)

Printed by CanPrint Communications Pty Ltd

Australian Government

Australian Reinsurance Pool Corporation

11 September 2007

The Hon Peter Costello MP
Treasurer
Parliament House
CANBERRA ACT 2600

Dear Treasurer

I have pleasure in presenting to you the Annual Report of the Australian Reinsurance Pool Corporation for the year ended 30 June 2007. The report has been prepared under section 9 of the *Commonwealth Authorities and Companies Act 1997* and in accordance with the Finance Minister's Orders made under that Act.

Subsection 9(3) of the Act provides that the report is to be tabled in each House of the Parliament as soon as practicable.

Yours sincerely

J I Gersh AM
Chair

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Report from the Chair

It is with great pleasure I present ARPC's annual report for 2006-07.

ARPC's financial record over the past four years is highly satisfactory. Total revenue has grown from $19.740 million in 2003-04 to $115.698 million in 2006-07. Total gross written premium over the four years of the scheme's operation amounts to $355.922. As at 30 June 2007 the reserve for claims stood at $332.01 million, up from $18.16 million in 2003-04.

Investment income has also experienced significant growth: from $0.53 million in 2003-04 to $18.80 million in 2006-07. ARPC will continue to pursue a prudent investment policy consistent with its obligations under the *Commonwealth Authorities and Companies Act 1997* and the need to ensure its funds are reasonably liquid if a call is made on them.

In addition to the increase in revenue and investment income, active treaty numbers have grown significantly. As at 30 June 2004, ARPC had 187 active treaties. That number had grown to 228 as at 30 June 2007.

ARPC will continue to ensure that insurance companies writing eligible insurance contracts are aware of the scheme established by the *Terrorism Insurance Act 2003* and ARPC's role in administering the scheme. The educative role undertaken by ARPC will include a continuation of its program to ensure industry participants are aware of the effect of the refinements to the scheme introduced by the review undertaken in 2006. These refinements include progressively increased company and industry retentions and changes to the way reinsurance premiums are calculated on bundled insurance premiums.

Consistent with Government policy, the refinements to the scheme are designed to encourage the re-emergence of the commercial terrorism market. The next review of the scheme is due to be completed by June 2009 and it is likely that 2009 review will include an evaluation of the effect of the scheme as a whole and the recently introduced refinements on the commercial terrorism insurance market.

Neil Weeks and I continue to work together to ensure that contact is maintained with industry and Government bodies in Australia and with various bodies overseas which perform a function similar to that of ARPC.

To this end, the attendance of Mr Weeks at various meetings of the OECD Network on the Financial Management of Large-scale Catastrophes and the High Level Advisory Board to the Network provides opportunities for ARPC to increase its awareness of developments in other OECD countries. It also ensures that ARPC is a part of a global network pursuing projects on the financial management and compensation of large-scale disasters, covering natural catastrophes, accidental man-made disasters and terrorist acts.

I continue to attend meetings of the Business-Government Advisory Group on National Security. My membership of this body has strengthened ARPC's relationships with industry and Government bodies concerned with security issues.

The Statement of Expectations and Statement of Intent contemplated by the *Review of the Corporate Governance of Statutory Authorities and Office Holders* (the Uhrig Report) are discussed at Chapter 3. However, it is pleasing to note from the Statement of Expectations that the Government considers that ARPC is a high performing and responsive advisory body.

In this connection, I would like to take this opportunity to thank and acknowledge the Chief Executive, Mr Neil Weeks, and his team for their professionalism and dedication. I should also like to thank the Members of the Board, Andrew Lumsden, Marian Micalizzi, James Murphy, Margot Rathbone and Geoff Vogt for their outstanding contributions.

I look forward to working with my fellow Members, the CEO and ARPC employees to ensure that ARPC remains a high performance and responsive advisory body.

J I Gersh AM
Chair
11 September 2007

Report from the Chief Executive

ARPC has again enjoyed a successful year, both financially and operationally, and the annual report highlights its achievements.

The overview contained in Chapter 1 of the annual report includes a discussion on ARPC's role and functions, the structure of the scheme and how premiums are calculated. Chapter 2 highlights some income and exposure information. ARPC's commitment to good corporate governance practice is documented in Chapter 3. The general information provided in Chapter 4 includes statutory reporting requirements not published elsewhere in the report.

The refinements foreshadowed by the *Terrorism Insurance Act Review: 2006* came into effect on 1 July 2007. ARPC continues to work to ensure that insurance companies which write eligible insurance contracts are aware of ARPC and the scheme it administers. In addition, ARPC has worked with clients and the wider industry to try to ensure that the implications of the refinements are understood. I wish to express my appreciation of the contribution of the industry, both to the design of the refinements and their implementation.

The refinements required amendments to be made to the reinsurance agreements between ARPC and its clients. Notices of amendment were issued to each client in March 2007. No other amendments have been made to the standard reinsurance agreement other than the modifications required to suit the particular circumstances of foreign insurers, dedicated insurance subsidiaries of corporate groups (captives) and Lloyd's syndicates.

During 2006-07 the cedant review program focussed on revisiting clients to discuss the implementation of recommendations made during the initial review. The program continues to produce positive results, for both ARPC and its clients. Consequently, ARPC intends to maintain the program. A new round of reviews will be designed for 2007-08 and those clients selected for review will be contacted to arrange a mutually convenient time for ARPC's review team to visit.

ARPC appreciates the opportunities afforded by the cedant review program for it to gain a greater understanding of the challenges faced by its clients, and for it to continue to inform and educate clients on ARPC and the operation of scheme.

The standard reinsurance agreement obliges each cedant to provide ARPC with an annual aggregate report. The report summarises the cedant's aggregate exposures to building, contents and business interruption risks at post code level. This information allows ARPC to analyse the distribution of exposure risk across Australia. The web-based submission of this information assists clients in the submission of the report and makes it easier for ARPC to analyse that data.

In addition to evaluating the annual aggregate reports, ARPC has undertaken considerable work towards developing loss estimation models which will enable it to estimate its potential exposure in the event of a declared terrorist incident. ARPC will continue to develop these models and will test the models using various disaster scenarios. ARPC will also foster alliances with industry bodies and other agencies which are undertaking similar work.

ARPC continues to publish its quarterly newsletter with a view to keeping clients and other stakeholders informed on ARPC, its operations and its product. The newsletter is posted on ARPC's website to ensure any interest party has easy access to relevant information.

I greatly appreciate the support and guidance afforded to me by the Chair and other Members. I also appreciate the confidence afforded to ARPC by the Government, clients and the industry more generally.

ARPC's success is due, in no small measure, to the hard work and dedication of its staff. To all staff members, I extend my thanks for your commitment and loyalty, both to the organisation and to me personally. I look forward to working with Members and my colleagues to ensure that ARPC maintains its high standards and good reputation.

N E Weeks
Chief Executive
11 September 2007

Report of operations

The Members of the Australian Reinsurance Pool Corporation are pleased to present their annual report on the operations of the Corporation for the financial year ended 30 June 2007. This report is made in accordance with a resolution of the Members.

The Members are responsible under section 9 of the *Commonwealth Authorities and Companies Act 1997* for the preparation and content of the report of operations in accordance with the Finance Minister's Orders.

Signed for and on behalf of Members in accordance with a resolution of the Members.

J I Gersh AM
Chair

11 September 2007

A J Lumsden
Member and Chair of the Audit and Compliance Committee
11 September 2007

Chapter 1: Overview

Role and functions

Background

The *Terrorism Insurance Act 2003* (TI Act) establishes a scheme for replacement terrorism insurance coverage for commercial property and business interruption. The scheme commenced on 1 July 2003.

The TI Act also establishes ARPC as a statutory authority to administer the scheme. ARPC began operations on 1 July 2003.

The terrorism reinsurance scheme established by the TI Act is the Government's response to the withdrawal of terrorism insurance cover following terrorist attacks around the world, particularly the events of 11 September 2001 in the United States of America. The scheme was introduced as a result of calls from the community for the Government to intervene in an area of clear market failure and after discussions with key industry stakeholders — including insurance and reinsurance companies, banks, representatives of property owners, industry associations, insurance brokers and actuaries.

Before introducing the scheme, the Government considered the broad economic impacts which could result from a large pool of assets uninsured for terrorism risk. The potential impacts included delaying commencement of investment projects and altering portfolio management decisions as banks and commercial property trusts became concerned with the amount of property without adequate cover. The Government was concerned that lack of comprehensive insurance cover for commercial property or infrastructure would lead to a reduction in financing and investment in the Australian property sector and that this would subsequently have wide economic impacts. These considerations led to the Government to conclude that intervention was necessary.

The Government decided that any intervention should be consistent with the need to:

- maintain, to the greatest extent possible, private sector provision of insurance;
- ensure that risk transferred to the Commonwealth is appropriately priced to minimise the impact on the Commonwealth's financial position;

- ensure that the Commonwealth is being compensated by those benefiting from the assistance;
- allow the commercial insurance and reinsurance markets to re-enter the market when they are able (that is, ensuring an appropriate exit strategy for Government); and
- be compatible with global solutions.

Consistent with the Government's intention that the scheme should operate only while terrorism insurance cover is unavailable commercially on reasonable terms, the TI Act includes a requirement for a review to be conducted, at least every three years, for the need for the TI Act to continue.

The first review was completed in June 2006. The review concluded that it appears unlikely that an adequate supply of terrorism risk insurance will return in the short to medium term in either the domestic or global markets at a reasonable price. Consequently, the Government accepted the recommendation that the TI Act continue in operation, subject to a further review in no more than three years. The next review is scheduled to be completed by 30 June 2009.

Legislative function

ARPC's function is to provide insurance cover for eligible terrorism losses (whether by entering into contracts or by other means).

ARPC has the power to do all things necessary or convenient to be done for or in connection with the performance of its functions, including:

- the power to charge premiums in respect of contracts of insurance for which it is the insurer; and
- the power to charge fees for services that it provides in connection with the performance of its functions.

Mission

ARPC's mission is to ensure that:

- all insurers of eligible insurance contracts have the opportunity to reinsure with ARPC for eligible terrorism losses; and
- the commitments under the reinsurance agreements are met in a timely manner.

Objectives

ARPC seeks to ensure that all issuers of eligible insurance contracts are aware of their exposure to eligible terrorism losses by virtue of the operation of the TI Act and that, if the exposure is not reinsured with ARPC, the insurer has made a conscious decision not to accept ARPC's offer of reinsurance.

A key objective is to ensure that ARPC is in a position to pay claims in an equitable and timely manner.

ARPC also considers that it should be in a position to advise on the magnitude of its probable losses in the event of a declared terrorist incident and, consequently, an appropriate reduction percentage.

With these ends in mind, ARPC has identified its objectives as:

- to promote the objectives of the TI Act;
- to meet the terrorism reinsurance needs of insurers writing eligible insurance contracts;
- to provide advice on current trends in the terrorism insurance market;
- to be in a position to pay claims efficiently in the event of a declared terrorist incident;
- to be in a position to accurately estimate the likely damage in the event of a declared terrorist incident and to give credible advice in relation to an appropriate reduction percentage;
- to operate successfully and efficiently;
- to be an employer of choice; and
- to assist in community based activities which employ and develop the professional skills of its staff.

The scheme

The TI Act effectively deems terrorism risk cover into eligible insurance contracts by rendering terrorism exclusions clauses void. Insurance companies may reinsure their additional risk with ARPC.

As terrorism exclusion clauses are rendered ineffective by the TI Act, payouts available to holders of eligible insurance contracts for terrorism losses depend on the underlying coverage in the eligible insurance contract. For example, if a terrorist act caused a fire, then a policyholder would be able to claim for subsequent loss if their insurance policy would normally cover damage from fire. Conversely, if a terrorist act involved biological contamination and the underlying insurance policy does not include cover for biological contamination, then the reinsurance provided by the scheme would not respond.

The compulsory application of the scheme to all eligible insurance contracts is essential to allow the accumulation of a credible pool of funds within a reasonable period. Universal terrorism insurance is also designed to avoid problems of undiversified risk (for example, insuring only high risk buildings) and uncertainty as to who will be eligible for compensation in the event of a declared terrorist incident.

Coverage

Contracts of insurance covered by the scheme are those that provide insurance for:

- loss of, or damage to, eligible property that is owned by the insured;
- business interruption and consequential loss arising from:
  - loss of, or damage to, eligible property that is owned or occupied by the insured; or
  - inability to use eligible property, or part of eligible property, that is owned or occupied by the insured; and
- liability of the insured that arises out of the insured being the owner or occupier of eligible property.

The TI Act includes (at section 5) a definition of *terrorist act*. In order to have consistency across Commonwealth legislation, the definition draws on the meaning of terrorist act contained in the Criminal Code. The Minister, in consultation with the Attorney-General, determines whether a terrorist act has happened in Australia. Once that determination has been made the Minister will announce a declared terrorist incident under section 6 of the TI Act. Upon that declaration, the provisions of the TI Act in respect of eligible terrorism losses become effective.

The scheme covers eligible terrorism losses for any declared terrorist incident covered by an eligible insurance contract where the insurer has a reinsurance agreement with ARPC. The TI Act excludes from the definition of eligible terrorism losses any loss or liability arising from the hazardous properties (including radioactive, toxic or explosive properties) of nuclear fuel, nuclear material or nuclear waste.

Coverage is available for Commonwealth and State business enterprises as well as Commonwealth-owned airports leased commercially. As a result of the 2006 review the scheme has been extended to include all public authorities which have taken out commercial insurance. Farms benefit from cover for terrorism risk if they hold insurance against business interruption. Private residential property is not included in the scheme.

The Regulations also exclude certain other types of insurance coverage, including: marine insurance, aviation insurance, motor vehicle insurance, life insurance, health insurance, private mortgage insurance, medical indemnity insurance, and professional indemnity insurance.

The pool

Insurance companies which write eligible insurance contracts may reinsure through ARPC the risk of claims for eligible terrorism losses. Premium income will build up ARPC's first layer of funds available to cover claims from declared terrorist incidents. The pool is supplemented by a bank line of credit of $1 billion, underwritten by the Commonwealth, as well as a Commonwealth indemnity of $9 billion.

ARPC's exposure is effectively capped at $10 billion plus the accumulated reserve for claims. This is done by way of the declaration by the Treasurer of a *reduction percentage* under section 6 of the TI Act.

Reduction percentage

If the Minister considers that, in the absence of a reduction percentage, the total amounts paid or payable by the Commonwealth under the guarantee contained in section 35 of the TI Act would exceed $10 billion, then the announcement of a declared terrorist incident must be accompanied by the specification of a reduction percentage. The effect of a reduction percentage is to reduce the amounts payable under eligible insurance contracts as a result of eligible terrorism losses. The reduction percentage may be varied, but only by making it smaller.

Retentions

Insurers who reinsure their terrorism risks through ARPC retain part of the risk of liability from a declared terrorist incident. As a result of the 2006 review, retentions have been increased. These increases take effect in three increments (respectively, from 1 July 2007, 1 July 2008 and 1 July 2009), as follows:

Date	Annual insurer retention		Maximum industry retention per incident
	Minimum	Maximum	
Pre 1 July 2007	Nil	The lesser of $1 million or 4 per cent of fire and ISR premiums collected	$10 million
1 July 2007	$100,000	The lesser of $1 million or 4 per cent of fire and ISR premiums collected	$25 million
1 July 2008	$100,000	The lesser of $5 million or 4 per cent of fire and ISR premiums collected	$50 million
1 July 2009	$100,000	The lesser of $10 million or 4 per cent of fire and ISR premiums collected	$100 million

The Ministerial direction in relation to these increases is discussed in Chapter 3.

Layers of the scheme

The scheme effectively provides a six-layer model that operates to spread the cost of any claims.

Layer	Element
First layer	Policyholder's liability for some risk through a possible excess or deductible
Second layer	Retention of some risk by insurers
Third layer	Pool of premiums paid to ARPC for reinsurance
Fourth layer	Commercial line of credit for $1 billion funded by the pool of premiums
Fifth layer	Commonwealth indemnity for up to $9 billion
Sixth layer	Possible liability for some risk by policyholder, through the operation of the reduction percentage or policy limits

As noted above, a commercial policy holder retains some risk. For example:

- there may be an excess or deductible set in the insurance policy;
- a commercial policy holder will not receive a full payout under the insurance policy if a reduction percentage is specified; and
- the actual loss may be greater than the upper limit of cover provided by the policy.

Premiums

The premium charged for reinsurance is determined by Ministerial direction. The premiums have been set having regard to the level of risk. There are three broad tiers based on geographic location and identified by postcode. Postcodes allocated to Tier A are those covering the CBD areas of Australian cities with a population of over 1 million (that is, Sydney, Melbourne, Brisbane, Perth and Adelaide). Postcodes allocated to Tier B are those covering the urban areas of all state capital cities and cities with a population of over 100,000 (that is, Sydney, Melbourne, Brisbane, Perth, Adelaide, Gold Coast, Canberra, Newcastle, Central Coast of New South Wales, Wollongong, Hobart, Geelong, Sunshine Coast of Queensland, Townsville and Darwin). Postcodes allocated to Tier C are those postcodes not allocated to either Tier A or B.

Any property not on the mainland of Australia or Tasmania, but within the coastal sea of Australia within the definition included in section 3 of the TI Act, is Tier C.

Reinsurance premiums are calculated as a percentage of the reinsured's gross base premium in accordance with the following table. There is also provision to increase the percentage after a declared terrorist incident in order to finance ARPC's liabilities and rebuild the pool.

Premium structure for reinsurance

Class of insurance	Tier	Initial rate from 1 October 2003 per cent	Maximum rate (after an event) per cent
Commercial property	A	12	36
	B	4	12
	C	2	6
Business interruption	A	12	36
	B	4	12
	C	2	6
Public liability		Nil	2

ARPC's premium and investment income is used to fund its operations and build the pool available to meet future claims. While the TI Act provides that the Minister may direct ARPC to pay dividends to the Commonwealth, no such payments have been required to date.

Premiums on bundled insurance policies

As a result of the 2006 review, a new Ministerial direction was issued instructing ARPC to charge reinsurance premiums on only those sections of a bundled insurance policy that exclude terrorism risks. A bundled insurance policy is one that:

(a) is comprised of two or more distinct covers that have been packaged or bundled together; and

(b) was offered on the basis that the insured must take out one or more of a number of covers offered; and

(c) precisely quantifies the premiums attributable to each cover comprising that contract of insurance; and

(d) contains covers that (if provided individually) would be an *eligible insurance contract*.

Organisational structure

The TI Act provides that the Members are the Chair and at least four, but not more than six, other Members. The Members are appointed by the Minister.

Members

Mr Joseph Gersh AM, Chair — appointed 1 July 2003

Mr Gersh was re-appointed to the position of part-time Chair for a period of three years commencing 1 July 2006.

Mr Gersh has extensive experience in law and commerce, and was a senior partner with Arnold Bloch Leibler from 1982 until his retirement from that position in 1999. Mr Gersh is the Executive Chairman of Gersh Investment Partners Limited and currently has a range of directorships, including the Payments System Board of the Reserve Bank of Australia.

Mr Andrew Lumsden — appointed 1 July 2003

Mr Lumsden was re-appointed to the position of part-time Member for a period of three years commencing on 1 July 2006.

Mr Lumsden is a Partner at Corrs Chambers Westgarth. He specialises in corporate and securities law and mergers and acquisitions. Mr Lumsden is an acknowledged expert in the field of corporate governance issues. From 1998 until 2001 he was Chief of Staff to the Minister for Financial Services & Regulation, the Hon Joe Hockey, MP. Prior to 1998 Mr Lumsden was a partner of Corrs Chambers Westgarth. Mr Lumsden is a member of the Takeovers Panel and a member of the Corporations Committee of both the Law Council of Australia and the Australian Institute of Company Directors. Mr Lumsden is also the Chair of the Audit and Compliance Committee.

Ms Marian Micalizzi — appointed 1 July 2003

Ms Micalizzi was re-appointed to the position of part-time Member for a period of three years commencing on 1 July 2006.

Ms Micalizzi is a chartered accountant with over 20 years experience, a company director and a consultant in both the public and private sector. Ms Micalizzi is a former partner of PricewaterhouseCoopers (until 2000) having been admitted as a partner of the predecessor firm in 1986. Ms Micalizzi sits on a number of boards, including the Queensland Investment Corporation and the Queensland Treasury Corporation. She is a member of the Corporations and Markets Advisory Committee and the Takeovers Panel and is a councillor of the Australian Institute of Company Directors (Qld Division). Ms Micalizzi is also a member of the Audit and Compliance Committee.

Mr James Murphy — appointed 1 July 2003

Mr Murphy was re-appointed to the position of part-time Member for a period of three years commencing on 25 April 2005.

Mr Murphy is the Executive Director, Markets Group in the Treasury. He has extensive experience with the Commonwealth Government, including holding senior positions with the Department of Finance as head of Budget Policy, with the Department of the Treasury as Principal Adviser, Corporations Law and with the Attorney-General's Department as head of the Business Law Division. Mr Murphy is also a member of the Audit and Compliance Committee.

Ms Margot Rathbone — appointed 25 April 2005

Ms Rathbone was appointed to the position of part-time Member for a period of three years commencing on 25 April 2005.

Ms Rathbone has more than 20 years experience in the reinsurance industry and has held senior positions with a number of reinsurance companies. Her most recent appointments include Managing Director of Aon Re and General Manager of Employers Reinsurance Corporation. Ms Rathbone has served as President and Committee Member of the Australian and New Zealand Institute of Insurance and Finance (NSW Branch) as well as President of the Reinsurance Discussions Group (NSW). She was also a committee member of the Reinsurance Study Course which designs and presents continuing education courses to insurance professionals.

Mr Geoffrey Vogt — appointed 29 August 2005

Mr Vogt was appointed to the position of part-time Member for a period of three years commencing on 29 August 2005.

Mr Vogt has extensive experience in the financial services and insurance industries. He is Chief Executive Officer of the Motor Accident Commission in South Australia, a statutory authority which has responsibility for the monopoly compulsory third party insurance scheme in that State. Mr Vogt is currently a member of the Centre for Automotive Safety Advisory Board. He is also a Commissioned Officer in the Australian Army Reserve having served for approximately 30 years in a variety of roles. Mr Vogt is a member of CPA Australia and an Associate of the Australian and New Zealand Institute of Insurance and Finance.

Chief Executive

The TI Act provides for the appointment by ARPC of a Chief Executive. The Chief Executive is responsible for the management of the affairs of ARPC subject to the directions of, and in accordance with policies determined by, ARPC.

Mr Neil Weeks has been ARPC's Chief Executive since the scheme was established on 1 July 2003. Mr Weeks has more than 30 years experience in the commercial insurance industry, having held senior positions both in Australia and overseas. He was the Chief Executive Officer of the Territory Insurance Office of the Northern Territory from 1993-2003. Mr Weeks has a degree in economics and a Master of Business Administration from Monash University and is a Fellow of CPA Australia, the Australian Institute of Company Directors and the Australian Institute of Management.

Other staff

ARPC may also employ those people it considers necessary for the performance of its functions and the exercise of its powers. As at 30 June 2006, ARPC had fifteen employees (including the Chief Executive). Twelve employees work full-time, two work part-time and one employee is on maternity leave. An organisational chart is attached at Appendix A.

Twelve employees are located in ARPC's Canberra office. Three employees are located in Sydney where ARPC shares premises with the Inspector-General of Taxation.

Chapter 2: Report on performance

Financial

Summary of financial information

Financial highlights

	2007	2006	2005	2004
	$'000	$'000	$'000	$'000
Net premium revenue	**96,890**	102,537	91,321	18,986
Acquisition costs	**(412)**	(930)	(532)	(198)
Investment income	**18,803**	10,833	4,790	532
Other income	**5**	15	-	-
Revenues from government	**-**	-	-	222
Other operating expenses	**(3,973)**	(3,034)	(2,467)	(1,378)
Operating result	**111,313**	109,421	93,112	18,164
Gross written premium	**94,729**	103,204	102,188	55,801
Expense ratio	**4.53%**	3.87%	3.28%	8.30%
Cash and cash equivalents	**91,508**	67,254	34,511	30,631
Investments	**263,000**	187,867	100,000	-
Reserve for claims	**332,010**	220,697	111,276	18,164

ARPC's 2006-07 financial result continues to build on the impressive financial achievements produced by ARPC since its inception on 1 July 2003. In its four years of operation, ARPC has written a total of $355.922 million in gross written premium; generated $34.958 million in investment income; built its holdings of cash and investments to $354.508 million and the reserve for claims has grown to $332.010 million.

ARPC continues to prudently manage its financial resources in line with its statutory obligations and the objectives outlined in chapter 1.

Gross written premium

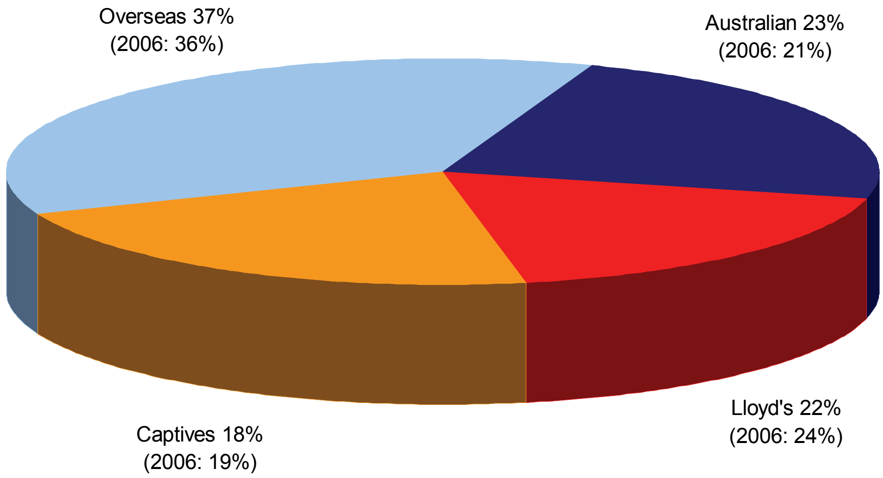
The gross written premium for the 2006-07 financial year was $94.729 million (2006: $103.204 million). The variation against the prior year's result was due mainly to two premium refunds totalling $5.782 million which, after investigation, ARPC agreed to refund. It should be noted the 2006-07 unclosed business estimate reduced to $22.430 million (2006: $24.294 million) as a result of the impact of the premium refunds.

The breakdown of gross written premium for 2006-07 is outlined in the following charts. ARPC will continue to monitor the quarterly returns, analysing the effects of market pricing on its gross written premium.

As at 30 June 2007 ARPC had 227 (2006: 221) active treaties in place. The gross written premium booked from the additional cedants was $0.331 million.

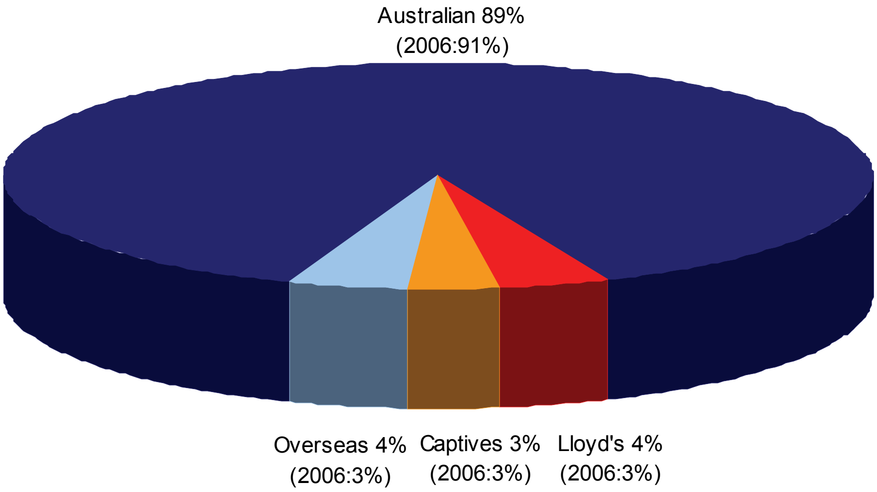
The proportion of Australian cedants increased slightly to 23 per cent while oversees cedants increased 1 per cent to 37 per cent, with corresponding reductions in the proportions of captives and Lloyd's syndicates.

Chart 1: Number of active treaties



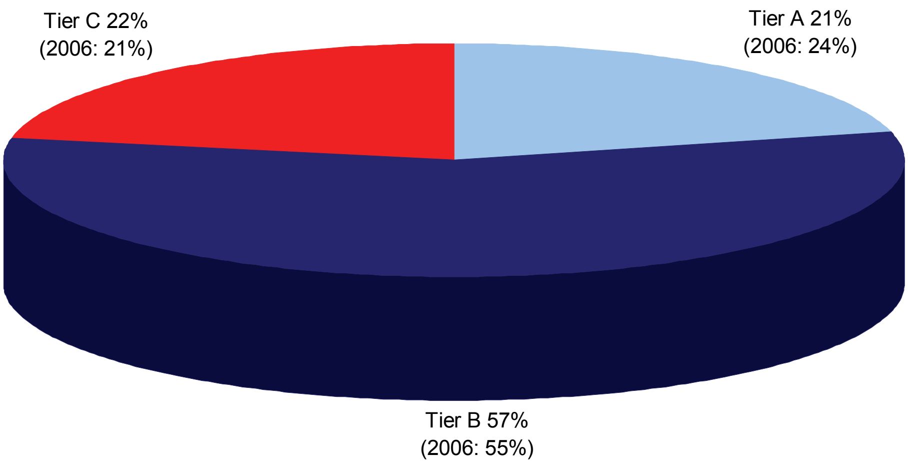
There has been a slight reduction of 3 per cent in the proportion of gross written premium attributable to Australian cedants.

Chart 2: Gross written premium by cedant type



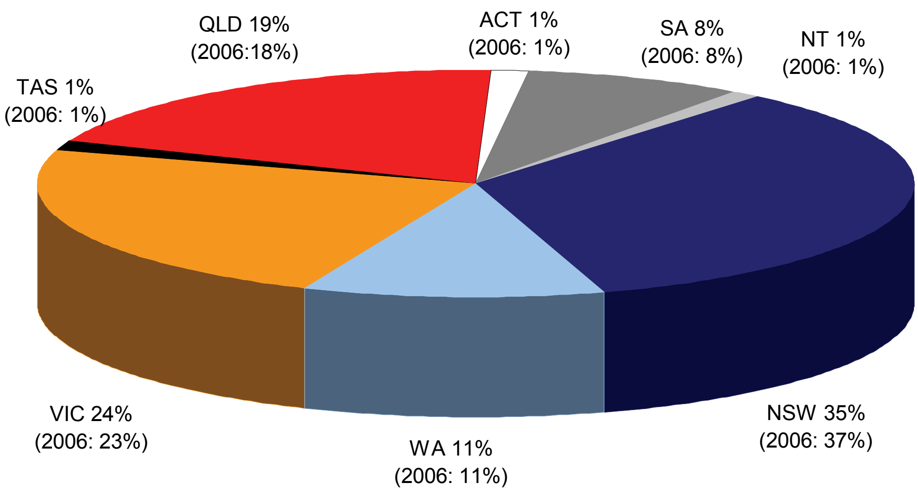
There was a slight variation in the collection pattern for tiers A, B and C with Tier A reducing by 2 per cent.

Chart 3: Gross written premium by tier



The relatively consistent pattern in the gross written premium collections is also apparent by State. NSW was the only state to register a decline (2 per cent) with both Victoria and Queensland registering a 1 per cent increase.

Chart 4: Gross written premium by State



Investment income

The following table provides a breakdown of ARPC's investment income as at 30 June 2007.

Investment income

For the period ended 30 June 2007

	2007 $'000	2006 $'000
Reserve Bank of Australia (RBA)		
Cash at bank	**2,546**	3,514
Fixed interest deposits	**9,351**	6,585
Total RBA income	**11,897**	10,099
External fund manager		
Cash at bank	**4,468**	228
Fixed interest deposits	**2,419**	479
Governement (guaranteed) securities	**19**	27
Total external fund manager income	**6,906**	734
Total invesment income	**18,803**	10,833

The growth in investment income continued to gather pace in 2006-07 with a result of $18.803 million (2005: $10.833 million). The major reasons for the increase were:

- the increasing size of the pool of funds;

- the continued increase in the use of fixed term deposits with the Reserve Bank of Australia;
- the appointment of a professional funds manager to manage a portion of funds on behalf of ARPC; and
- two increases in official interest rates during 2006-07.

The following table provides a breakdown of ARPC's cash and investment balances as at 30 June 2007.

Cash and investment balances

As at 30 June 2007

	2007 $'000	2006 $'000
Reserve Bank of Australia (RBA)		
Cash at bank	**37,583**	32,931
Fixed interest deposits	**160,000**	110,000
Total RBA cash and investments	**197,583**	142,931
External fund manager		
Cash at bank	**53,925**	34,323
Fixed interest deposits	**103,000**	66,000
Governement (guaranteed) securities	**-**	11,867
Total external fund manager cash and investments	**156,925**	112,190
Total cash and investments	**354,508**	255,121

ARPC manages its investments within a conservative framework. ARPC's objectives are to ensure that:

(a) the investment strategy complies with the *Commonwealth Authorities and Companies Act 1997* in relation to investing ARPC's surplus funds, including all investments being held in ARPC's name;

(b) capital stability of the funds is maintained;

(c) funds are available at short notice; and

(d) the fund is returning a rate of return acceptable to the Board. The Board approved benchmark return for ARPC is the official cash rate.

In May 2006 the Board approved allocation of $100 million was transferred to the external fund manager with a subsequent allocation of $50 million approved and transferred in May 2007. All bank accounts managed by the external fund manager are held in ARPC's name.

In 2005-06 ARPC received advice from the Department of Finance and Administration, the Australian Government Solicitor, the Department of the Treasury and the

Australian National Audit Office that the arrangement with the external fund manager complies with section 18 of the CAC Act.

Expenses

ARPC's expense ratio for 2006-07 was 4.53 per cent (2006: 3.87 per cent). The increase is attributable to the following:

- a reduction in the net premium revenue;
- an increase in employee expenses represented by an additional staff member, part-time staff increasing the hours worked and general pay reviews;
- additional expenses relating to the development of the loss exposure model and the expensing of deferred acquisition costs from 2005-06; and
- an increase in the depreciation and amortisation expense.

ARPC continues to tightly control expenses, ensuring it receives value for money from its service providers and is in a position to meet its statutory obligations.

Influences on future performance

The reinsurance premiums collected by ARPC are dependent on the underlying premiums charged by its cedants. Any softening of those underlying premiums will have a negative effect on ARPC's premium income.

ARPC relies on its cedants to return the correct amount in reinsurance premiums. The incorrect calculation of premiums could have a negative effect on ARPC's premium income. ARPC's cedant review program addresses, inter alia, the identification of eligible insurance contracts for the purpose of ceding terrorism reinsurance premium to ARPC and premium calculation and remittance.

Any movement in interest rates will have an impact on ARPC's investment income.

Exposure Risk Management

ARPC objective

One of ARPC's objectives is to be in a position to accurately estimate its likely exposures in the event of a declared terrorist incident (DTI) and to give credible advice in relation to an appropriate reduction percentage.

The Government also expects ARPC to seek to be in a position to advise the responsible Treasury Minister of likely costs to ARPC in the event of a DTI. The Statement of Expectations received from the Parliamentary Secretary to the Treasurer is discussed in Chapter 3.

Background

When ARPC first entered the terrorism reinsurance market in July 2003, it did not have the ability to estimate losses from a potential terrorist attack. To address this issue ARPC implemented a strategy to enable it to develop the capability to accurately estimate its possible exposures in the event of a DTI and provide credible advice to the Government on an appropriate reduction percentage.

Details of the work undertaken by ARPC to meet its objective and fulfil the Government's expectations follow.

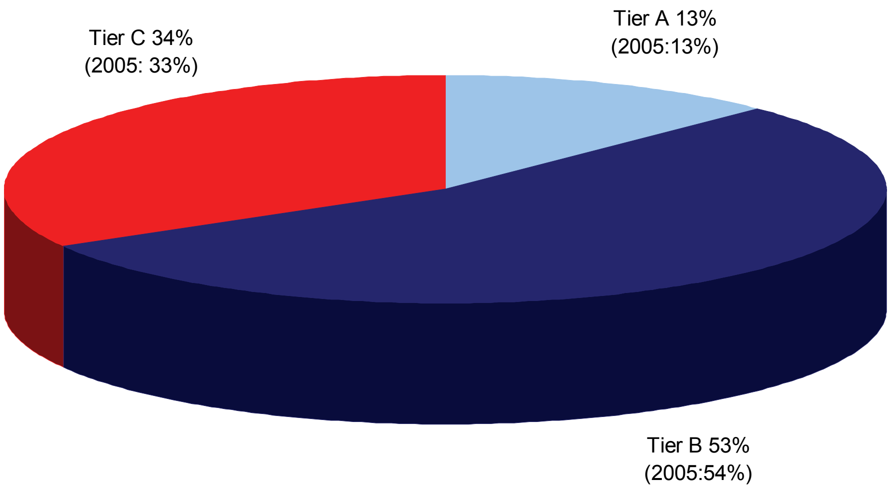
ARPC risk aggregator system

Each cedant is required under clause 10(b) of the reinsurance agreement to provide an annual aggregate report. The report summarises the cedant's aggregate exposure amounts at a post code level and is split into buildings, contents and business interruptions risks. This exposure information is considered important in allowing ARPC to analyse the distribution of exposure risk across Australia.

A web-based reporting system was developed to facilitate the submission of reports by cedants and allow ARPC to quickly obtain reports based on the large volume of data provided by cedants.

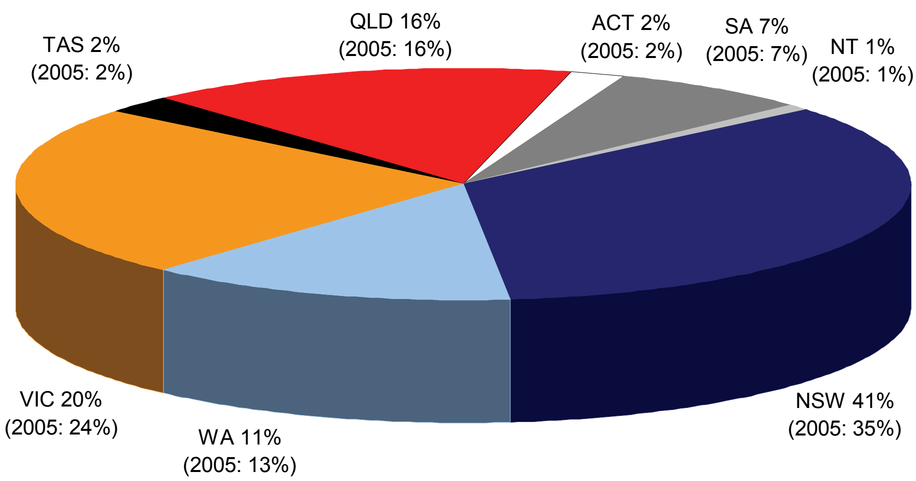
The following charts provide an overview of ARPC's total exposure for 2006 based on information provided by cedants. The largest gross exposure is recorded in Tier B at 53 per cent, with Tier A accounting for 13 per cent.

Chart 5: Aggregate exposure by tier as at 30 June 2006



There is a general correlation between the aggregate exposure by State and the premium collection by State. Victoria cedes 24 per cent of premium and represents 20 per cent of aggregate exposure, while NSW cedes 35 per cent of premium and represents 41 per cent of aggregate exposure.

Chart 6: Aggregate exposure by State as at 30 June 2006



Loss estimation modelling

Initial loss estimation model

One of ARPC's first priorities was to build a loss estimation model. The initial modelling work was completed in conjunction with Finity Consulting.

This model uses average floor area values for high rise buildings, the expected contents values by floor, an average business interruption figure and the known maximum public liability sum insured.

No further development is expected to be undertaken on this model.

MapInfo loss estimation model

ARPC progressed from its initial model to the Mapinfo model. The Mapinfo system is a spatial application that captures and graphically displays geographical details and other relevant information.

Through its good relationships with cedants, ARPC sought and received detailed information from selected cedants. This data has been geo-coded in MapInfo and utilised in scenario tests.

ARPC will approach cedants again during 2007-08 seeking updated data. ARPC recognises and appreciates that cedants provide this information on a voluntary and confidential basis.

Additional work will be undertaken to incorporate damage foot-prints into the MapInfo database.

Continued development

During 2006-07 Risk Frontiers of Macquarie University commenced work on an enhanced loss estimation model. This model incorporates the main characteristics of the MapInfo system plus data for some capital city centres and will eventually have the capacity to model other exposures such as associated business interruption from major infrastructure losses. ARPC is working with Risk Frontiers and Finity Consulting to ensure the reasonableness of the assumptions on which the model is built.

Stage 1 of this model has been completed. The model superimposes damage footprints over CBD cadastral maps and calculates estimated loss values for each land parcel. The loss estimate is then fine-tuned by adjusting the damage footprint based on actual damage reported from the subject locations. Estimates can be categorised between buildings, contents, business interruption and public liability. Additional development will continue to extend and enhance the model.

ARPC will continue to foster co-operative relationships within the industry and government to fully utilise available expertise and resources in the development of its loss estimation modelling capabilities.

Non-financial

Outcomes and outputs

ARPC measures itself against the objectives (both financial and non-financial) identified in its business plan. The business planning process is conducted towards the end of each financial year and measures the outcomes from the current financial year and sets targets for the coming financial year. The business plan is presented to the Members for discussion and endorsement at their last meeting in the current financial year, which is usually scheduled for the last week in June.

ARPC has developed a balanced scorecard as a means of measuring its financial and non-financial performance. The components of the balanced scorecard are:

(a) financial;

(b) corporate governance;

(c) growth;

(d) monitoring service level agreements;

(e) human resource management;

(f) client satisfaction; and

(g) social/community.

Within each component, key performance indicators measure ARPC's performance against set targets.

The balanced scorecard is produced and issued monthly. It is included in the Chief Executive's report to the Board.

Awareness campaign

Since its inception ARPC has undertaken, and will continue, an extensive industry awareness campaign to ensure that all insurers are aware of the scheme and their obligations under it and to offer reinsurance contracts to all those insurers which write eligible insurance contracts. The awareness campaign includes initiating and maintaining contact with industry bodies, delivering presentations and addresses to industry bodies and individual insurers and conducting an advertising campaign both in Australia and overseas.

ARPC will continue to communicate its offer of reinsurance to the market by giving presentations to local bodies such as the Insurance Council of Australia, Reinsurance Discussion Group, the Australian and New Zealand Institute of Insurance and Finance and at other forums it considers appropriate. Contact with foreign insurers and captives have been made by way of industry advertisements and presentations given to overseas markets and brokers.

ARPC has worked closely with the industry and clients to ensure there is awareness of the changes made to the scheme as a result of the *Terrorism Insurance Act Review: 2006*. ARPC will do as much as it can to assist clients in their understanding of the impact any changes may have on their business. This cedant review program is a vital tool in the provision of this assistance by ARPC to individual insurance companies.

Market coverage

Through the feedback received from the awareness campaign and the cedant review program, ARPC is confident that all insurers which write eligible insurance contracts have had the opportunity to reinsure their terrorism risk with ARPC.

A number of companies have entered into reinsurance agreements with ARPC but do not remit premium. This is due to an element of retrospectivity in ARPC’s standard reinsurance agreement. If a company has a contract of reinsurance with ARPC and incurs a liability solely because of section 8 of the TI Act, it is entitled to cover under the reinsurance agreement provided it complies with the terms of the agreement and pays the relevant premium (whether or not it was obvious or apparent that the contract under which it incurs a liability was an eligible insurance contract under the TI Act).

Significant events

No significant events occurred during the year which required notification to the Minister under section 15 of the *Commonwealth Authorities and Companies Act 1997*.

There have been no developments since the end of the 2006-07 financial year which has significantly affected or may significantly affect:

(a) ARPC's operations in future financial years;

(b) the results of those operations in future financial years; or

(c) ARPC's state of affairs in future financial years.

Chapter 3: Management and accountability

Corporate governance

Members

ARPC has a part-time non-executive Chair and five other part-time non-executive Members. All Members are appointed by the Minister.

The Members who held office at the date of this report, and during the period covered by this report, are:

Mr Joseph Gersh AM, Chair — appointed 1 July 2003 (current term expires 30 June 2009);

Mr Andrew Lumsden — appointed 1 July 2003 (current term expires 30 June 2009);

Ms Marian Micalizzi — appointed 1 July 2003 (current term expires 30 June 2009);

Mr James Murphy — appointed 1 July 2003 (current term expires 24 April 2008);

Ms Margot Rathbone — appointed 25 April 2005 (current term expires 24 April 2008); and

Mr Geoff Vogt — appointed 29 August 2005 (current term expires 28 August 2008).


Back row: Joe Gersh (Chair), Geoff Vogt, Andrew Lumsden, Jim Murphy
Seated: Neil Weeks (CEO), Margot Rathbone, Marian Micalizzi

There were six meetings of Members held during 2006-07. The table below sets out the number of meetings attended by each Member.

Name	Number of meetings entitled to attend	Number of meetings attended
Mr Joseph Gersh AM	6	6
Mr Andrew Lumsden	6	6
Ms Marian Micalizzi	6	6
Mr James Murphy	6	6
Ms Margot Rathbone	6	6
Mr Geoff Vogt	6	6

Corporate governance practices

ARPC is committed to following corporate governance best practice. To this end, it monitors developments in corporate governance from a range of sources, including the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission, the Australian Stock Exchange (ASX) and the Australian National Audit Office (ANAO). While ARPC is not regulated by APRA, it considers that APRA's standards for general insurers represent best practice and benchmarks itself against those standards.

ARPC has documented its corporate governance framework in a board charter, the terms of reference of its committees and the delegations to the Chief Executive.

While ARPC is not bound by the ASX's *Principles of Good Corporate Governance and Best Practice Recommendations*, it has used those principles as benchmarks to evaluate its corporate governance practices. The principles below are those contained in the ASX' *Principles of Good Corporate Governance and Best Practice Recommendations* released in March 2003. The second edition of the principles (*Corporate Governance Principles and Recommendations*) released on 2 August 2007 will be reviewed by ARPC during 2007-08. While the effective date for the revised principles is an entity's first financial year commencing on or after 1 January 2008, ARPC intends to report against the revised principles in its 2007-08 annual report.

Principle 1 – Lay solid foundations for management and oversight

- The roles and responsibilities of Members have been documented in a board charter.
- The charter was reviewed by Members in 2006-07.
- The delegation of powers and functions to the Chief Executive has been documented in a delegations authority.
- Certain matters are reserved for Members.

Principle 2 – Structure the board to add value

- A majority of Members are independent.
- The Chair is an independent Member.
- Different individuals exercise the roles of Chair and Chief Executive.
- A nominations committee is not necessary because the TI Act provides that Members are appointed by the responsible Minister.

Principle 3 – Promote ethical and responsible decision-making

- The Members have adopted a code of conduct which is documented in the board charter.
- Employees are bound by ARPC's code of conduct and values which have been formally documented.
- ARPC's fraud control plan gives guidance on the responsibility and accountability of employees for reporting and investigating reports of unethical practices.

Principle 4 – Safeguard integrity in financial reporting

- The Chief Executive and Chief Financial Officer state in writing to the Members that the financial reports present a true and fair view, in all material respects, of ARPC's financial condition and operational results and are in accordance with relevant accounting standards.
- An audit and compliance committee has been established.
- The audit and compliance committee consists of a majority of independent Members.
- The chair of the audit and compliance committee is an independent Member who is not the chair of the board.
- The committee has formal terms of reference.

Principle 5 – Make timely and balanced disclosure

- Media releases, announcements and ARPC's annual report are available on its website.
- ARPC's annual report is given to the responsible Minister and tabled in both Houses of Parliament in accordance with the provisions of the *Commonwealth Authorities and Companies Act 1997*.

Principle 6 – Respect the rights of shareholders

- ARPC does not have shareholders. However, it maintains good working relationships with its stakeholders (clients and government).

Principle 7 – Recognise and manage risk

- ARPC has documented its risk management policy and strategy.
- It has identified, assessed and documented its risks and has policies in place to minimise and manage those risks.
- The Chief Executive and the Chief Financial Officer state to the Members in writing that:
  - the statement given by them regarding the integrity of the financial statements is founded on a sound system of risk management and internal compliance and control which implements the policies adopted by the Members; and
  - ARPC's risk management and internal compliance and control system is operating efficiently and effectively in all material respects.

Principle 8 – Encourage enhanced performance

- During 2006-07 the Members conducted an internal evaluation of their performance. The evaluation addressed such issues as strategy and planning, board structure and role, meeting effectiveness, quality of information and performance monitoring.
- The results of that review were discussed at the board meeting held on 24 April 2007.
- The Members assess the performance of the Chief Executive against key performance indicators.
- The Chief Executive has designed a performance management system for all other staff members, including senior management.

Principle 9 – Remunerate fairly and responsibly

- Members' remuneration is determined by the Remuneration Tribunal.
- Remuneration packages for employees are determined having regard to salaries payable for similar positions within the public and private sectors.

Principle 10 – Recognise the legitimate interests of stakeholders

- ARPC regularly consults those with an interest in its operations, including industry associations, government agencies and clients.

Right to legal advice

With the consent of the Chair, Members have the right to seek independent advice, including legal, accounting and financial advice, at ARPC's expense. The terms of reference of each committee authorises the committee to take whatever independent advice it considers necessary.

Committees

ARPC has established two committees, the Audit and Compliance Committee and the Risk Committee. Both committees have terms of reference which were approved and adopted by Members. The terms of reference govern the powers, composition, duties and responsibilities of each committee and the conduct of committee meetings. The terms of reference of each committee were reviewed by Members during 2005-06.

Audit and Compliance Committee

The purpose of the Committee is to:

(a) assist the Board to:

(i) fulfil its responsibilities in relation to ARPC's accounting and financial reporting obligations;

(ii) comply with ARPC's statutory obligations;

(iii) oversee the work of the internal auditors; and

(b) provide a forum for communication between Members, the senior management of ARPC, the internal auditor and ANAO.

The members of the Committee are:

Mr Andrew Lumsden, Chair;

Ms Marian Micalizzi; and

Mr James Murphy.

Miarian Micalizzi, Andrew Lumsden, Jim Murphy

There were three meetings of the Committee held during 2006-07. The table below sets out the number of meetings attended by each Committee member.

Name	Number of meetings entitled to attend	Number of meetings attended
Mr Andrew Lumsden	3	3
Ms Marian Micalizzi	3	3
Mr James Murphy	3	3

Risk Committee

The purpose of the Committee is to:

(a) review and endorse ARPC's risk management framework to ensure that appropriate strategies are in place for identification, assessment and mitigation of risk;

(b) identify and understand the risks faced by ARPC in meeting its goals;

(c) ensure that management monitors the effectiveness of the risk management and control system; and

(d) encourage the adoption of an effective risk management culture within ARPC.

The Members consider that risk is a matter for the board as a whole. However, a Risk Committee has been established to ensure that risk is considered as a separate issue and not merely as another agenda item at a meeting of Members. All Members are members of the Committee and one of its main tasks is to review (at least annually) ARPC's risk management strategy.

There were two meetings of the committee held during 2006-07. The table below sets out the number of meetings attended by each Committee member.

Name	Number of meetings entitled to attend	Number of meetings attended
Mr Joseph Gersh AM	2	2
Mr Andrew Lumsden	2	2
Ms Marian Micalizzi	2	2
Mr James Murphy	2	2
Ms Margot Rathbone	2	2
Mr Geoff Vogt	2	2

Uhrig report

On 6 March 2006 ARPC received a letter from the Parliamentary Secretary to the Treasurer advising that the assessment of the governance arrangements for ARPC against the principles and templates outlined in the *Review of the Corporate Governance of Statutory Authorities and Office Holders* (the Uhrig report) had been completed. The outcome of the assessment is that the board template and the *Commonwealth Authorities and Companies Act 1997* will continue to apply to ARPC.

ARPC received a Statement of Expectations from the Parliamentary Secretary to the Treasurer on 3 May 2007. The statement outlined the Government's expectations of ARPC in the areas of its role and responsibilities, its relationships with the Minister, Treasury and clients, transparency and accountability, operational issues and its contribution to the review process required by the TI Act. ARPC responded to the Statement of Expectations with its Statement of Intent which was issued by the Chair on 24 July 2007.

The statement of intent outlines how ARPC intends to undertake its operations and how its approach to operations will be consistent with the Government's expectations. There is no inconsistency between the Government's expectations as outlined in the Statement of Expectations and ARPC's approach to its operations as outlined in the Statement of Intent.

The Statement of Expectations is attached at Appendix B and the Statement of Intent is attached at Appendix C. Both statements are published on ARPC's website under the 'Corporate Governance' navigation aid.

Code of conduct

The Members have adopted a code of conduct by which they have agreed to be bound. The code provides that Members must:

(a) exercise the powers and discharge the duties of office:

  (i) with due care and diligence;

  (ii) in good faith in the best interests of ARPC; and

  (iii) for a proper purpose;

(b) not improperly use their position;

(c) not improperly use information gained as a result of holding the position;

(d) act honestly and ethically;

(e) not allow personal interests, or the interests of any other person or organisation, to influence their conduct;

(f) bring an independent judgment to bear on all matters considered by the board;

(g) not engage in conduct likely to discredit ARPC;

(h) treat fellow Members and ARPC's employees with courtesy and respect; and

(i) comply with the spirit, as well as the letter, of the law.

Internal audit

ARPC has appointed Ernst & Young as its internal auditors. Ernst & Young undertook the following audit work for ARPC during 2006-07:

(a) a high level review of ARPC's business continuity plan against ANAO and global best practice;

(b) a review of ARPC's investment strategy and policy;

(c) a review of the premium collection process; and

(d) an administrative functions review, including management of ARPC's service level agreement with Treasury.

During 2005-06, and in consultation with management and the Audit and Compliance Committee, Ernst & Young developed an internal audit program for 2006-2009. In addition to general audit management, the detailed plan for 2007-08 provides for the following audit reviews to be undertaken:

(a) the preparedness of ARPC to respond to a terrorist incident;

(b) a review of ARPC's business risk assessments and mitigation strategies;

(c) ARPC's investment controls;

(d) the premium collection process, including IT security;

(e) ARPC's procurement and contracting policies; and

(f) the quality and timeliness of management reports to the Board.

Risk management

During 2006-07 ARPC reviewed its risk management policy and risk management strategy. It also updated its risk register after reviewing the identification, assessment and mitigation strategies developed in 2005-06. The updated risk register was tabled at the Risk Committee meeting held on 24 April 2007.

Risk identification, assessment and analysis will be conducted for any proposed new project, business process or system. Mitigation strategies will be developed for any risk identified and the risk register will be updated to include newly identified risks.

During 2007-08 ARPC will conduct a workshop to review its identified risks and the effectiveness of its mitigation strategies.

Business continuity

During 2006-07 a new business impact analysis was conducted. From that analysis ARPC updated its business continuity plan. Ernst & Young reviewed the plan against ANAO standards and global best practice.

Development and testing of the business continuity plan will continue during 2007-08 and it will be reviewed as part of the 2008-09 internal audit program.

Promoting an ethical working environment

Employees are bound by ARPC's code of conduct and values which have been formally documented.

ARPC promotes an ethical work environment by which it encourages staff to:

- strive for excellence;
- value teamwork, consultation and sharing ideas;
- value diversity among its people;
- treat everyone with respect;
- exhibit honesty in all their dealings; and
- treat colleagues with fairness.

With assistance from Ernst & Young, and in accordance with the *Commonwealth Fraud Control Guidelines (2002)*, ARPC developed a fraud control plan. The plan includes policies, procedures and guidelines to advise staff of the steps to be taken if a fraud is suspected or a breach of ARPC's code of conduct is alleged. The policies include whistleblower protection.

The plan will be reviewed during 2007-08 and fraud awareness training will be conducted.

Cedant review program

ARPC's cedant review program was introduced with the intention of assisting clients to meet their obligations under the reinsurance agreement. The philosophy behind the program is to further strengthen the relationship between ARPC and its clients. This is achieved by assisting clients to raise their awareness of the processes involved in the identification of eligible insurance contracts, premium calculation, premium remittance, aggregate reporting and claims procedures. ARPC has found all clients to be extremely receptive, helpful and co-operative. The program has achieved its objective of enhancing the collegiate relationship between ARPC and its clients.

In the first two years of the program, reviews of all Australian, New Zealand, Singaporean and Irish cedants as well as many Lloyd's syndicates were conducted. The results of the reviews revealed few systemic problems. Consequently, ARPC changed the focus of the program. During 2006-07 the program concentrated on revisiting cedants where agreement has been reached about the implementation of recommendations made during the initial review. This stage of the program is expected to be completed in 2007-08.

Because of the positive outcomes achieved by the cedant review program, ARPC intends to maintain the program. To this end, a new program will be designed with a view to continuing to foster the positive relationships ARPC has developed with clients.

Members' appointment and remuneration

Members are appointed in writing by the Minister. All appointments are on a part-time basis and the period of appointment must not exceed four years. The Minister must not appoint a person as a Member unless the Minister is satisfied that the person:

(a) has suitable qualifications and experience; and

(b) is of good character.

Members' remuneration is set by the Remuneration Tribunal.

Role of the responsible Minister

The Minister responsible for ARPC is the Treasurer, the Hon Peter Costello, MP. The Minister appoints ARPC's members.

Members will continue to report formally to the Minister through their annual report of operations.

The TI Act permits the Minister to give written directions to ARPC in relation to the performance of its functions and the exercise of its powers. The Minister issued two new directions to ARPC during the year ended 30 June 2007. Effective from 1 July 2007, the new directions replaced the Ministerial directions issued on 30 September 2003.

The directions in force for the 2006-07 financial year and their effect are set out below.

- A direction in respect of the risk to be retained by reinsureds.

  The effect of this direction is that for all declared terrorist incidents which occur during the same financial year, the risk to be retained by a reinsured is an amount equal to the lesser of $1 million or 4 per cent of the gross fire/industrial special risks premium revenue. If all retentions in respect of a single declared terrorist incident would otherwise exceed $10 million, the retentions will be reduced proportionately. The effect of this reduction is to limit the retention for all reinsureds in relation to a single declared terrorist incident to $10 million.

- A direction in respect of premiums.

  The effect of this direction is to set the premium rates to be charged by ARPC under its reinsurance contracts. The rates are set as a percentage of the gross base premium written by a reinsured in respect of eligible insurance contracts according to the postcode tier in which the eligible property is situated.

The directions in force from 1 July 2007and their effect are set out below.

- A direction in respect of the risk to be retained by reinsureds.

  The effect of this direction is that for all declared terrorist incidents which occur during the same financial year, the risk to be retained by a reinsured is an amount equal to the lesser of the *default figure*, 4 per cent of the gross fire/industrial special risks premium revenue or the *minimum retention*. If all retentions in respect of a single declared terrorist incident would otherwise exceed the *maximum industry* *retention*, the retentions will be reduced proportionately. The effect of this reduction is to limit the retention for all reinsureds in relation to a single declared terrorist incident to the *maximum industry retention*.

The *default figure* is to increase progressively as follows:

1 July 2007 to 30 June 2008 — $1 million

1 July 2008 to 30 June 2009 — $5 million

occurring after 30 June 2009 — $10 million

The *minimum retention* is set at $100,000.

The *maximum industry retention* is to increase progressively as follows:

1 July 2007 to 30 June 2008 — $25 million

1 July 2008 to 30 June 2009 — $50 million

occurring after 30 June 2009 — $100 million

- A direction in respect of premiums.

  The effect of this direction is to set the premium rates to be charged by ARPC under its reinsurance contracts. The rates are set as a percentage of the gross base premium written by a reinsured in respect of eligible insurance contracts according to the postcode tier in which the eligible property is situated. The direction also instructs ARPC to charge reinsurance premiums on only those sections of a bundled insurance policy that exclude terrorism risks.

The responsible Minister has not notified ARPC of any general policies of the Australian Government that are to apply to ARPC by virtue of section 28 of the *Commonwealth Authorities and Companies Act 1997*.

Chapter 4: General information

Human resource management

All employees are employed on fixed term contracts. The fixed terms contracts of all employees, other than the Chief Executive, are due to expire on 30 June 2009. This date coincides with the date on which the next review of ARPC and its legislation is likely to occur. These employees also benefit from individual Australian workplace agreements which sets out the employee's terms and conditions of employment.

The Chief Executive is employed on an individual fixed term contract. His term of office is due to expire on 31 March 2009.

ARPC has outsourced many of its human resource management functions to Treasury through a service level agreement. The functions outsourced include payroll, occupational health and safety and recruitment procedures.

ARPC's performance management system is a tool to assist ARPC to improve its organisation capability. It provides a mechanism for performance review and feedback, coaching, skills development, reward and recognition.

There is one formal appraisal in each year. An informal discussion is conducted between formal appraisals. The purpose of this discussion is to consider how the employee is performing against the benchmarks agreed at the formal appraisal, to identify any impediments to performance and means to overcome those impediments.

In additional to the formal and informal appraisals, managers assist employees by providing regular feedback and coaching and by identifying and encouraging appropriate career development opportunities.

Training and development

ARPC recognises the value of investing in employee and career development to maximise the performance of ARPC and its attractiveness as an employer.

ARPC is committed to employee training and development including leadership development, skills development training and relevant technical training and support. It also supports employee attendance at industry conferences, seminars and external courses.

ARPC provides support, in the form of leave and financial assistance, to employees undertaking part time courses of study that will enhance their contribution to ARPC. Studies assistance is an integral part of ARPC's human resources strategy, as it responds to the employee development needs identified through such means as corporate planning, performance management and career development processes.

ARPC has an agreement with the Australian and New Zealand Institute of Insurance and Finance, a leading provider of insurance education, training and professional services, to provide employees with an online learning facility *InSite*. The InSite Continuing Education and Learning Management System has been developed specifically to address the ongoing education and training requirements in the financial services reform environment. ARPC encourages employees to use the InSite learning facility to further develop their knowledge in insurance and finance.

Occupational health and safety

ARPC is committed to providing a safe and healthy workplace for all its employees. It will take all reasonable, practical, effective and efficient steps to do so.

ARPC's occupational health and safety (OH&S) function has been outsourced to Treasury through a service level agreement. Treasury's OH&S policy is designed to foster and maintain a safe and healthy working environment in accordance with the *Occupational Health and Safety (Commonwealth Employment) Act 1991*. One of ARPC's employees is a member of Treasury's OH&S Committee. The OH&S Committee meets quarterly to discuss occupational health and safety issues and policies, employee wellbeing, health and safety performance reporting, accommodation issues and accident and incident reports.

During 2006-07, ARPC received no accident or incident reports which resulted in a compensation claim. ARPC's policy is to thoroughly investigate all reported incidents and to take action to ensure employee health and safety is not compromised.

During 2006-07, no directions were given under section 45 and no notices were given under sections 29, 46 or 47 of the *Occupational Health and Safety (Commonwealth Employment) Act 1991*.

ARPC's health and safety representative conducts quarterly workplace inspections to identify and help rectify workplace hazards such as slippery walking surfaces, poor lighting and obstructed passageways. Reports on these inspections are given to Treasury's OH&S Officer.

ARPC employees have access to Treasury's employee assistance program provided by Davidson Trahaire Corpsych. This program provides confidential counselling on work-related and personal matters to employees and their families. Six-monthly reports allow Treasury's OH&S Committee to monitor use and identify workplace issues that need addressing. The employee assistance program also provides managerAssistTM, a consultative resource for employee management issues including advice on people management.

Free flu vaccinations were offered to employees during 2006-07.

Workplace diversity

Workplace diversity program

ARPC's workplace diversity and equal employment opportunity policies are covered by its service level agreement with Treasury.

ARPC is committed to implementing workplace diversity. As part of this commitment, ARPC will implement the strategies and initiatives of Treasury's Workplace Diversity Program which seeks to foster an environment that attracts, develops, values and retains people from varying cultural backgrounds as well as those of different ages, gender, talents, experiences, perspectives and backgrounds.

In implementing the workplace diversity program ARPC will seek to:

- ensure all employees practise and promote workplace diversity principles and objectives;
- ensure the recruitment process reflects workplace diversity principles;
- promote an environment where all employees are given the opportunity to develop to their full potential;
- create an environment where employees have the opportunity to balance their work and personal life style choices; and
- encourage and support a safe and healthy working environment.

ARPC has a number of family friendly and work/life balance practices, including flexible working arrangements and leave. In 2005-06, three of ARPC's 13 employees worked part-time.

Disability action plan

ARPC provides reinsurance to insurers writing eligible insurance contracts. Its role requires limited contact with the general public and it does not formulate policy. However, ARPC recognises the necessity of ensuring that people with disabilities have an equal opportunity to access information regarding its activities and to have access to its premises as appropriate.

As an equal employment opportunity employer, ARPC recognises the importance of ensuring that people with disabilities are able to access information about employment opportunities with ARPC, and are able to compete for such opportunities on an equal basis through the merit selection process.

ARPC has adopted and applies the principles contained in Treasury's Disability Action Plan.

Indemnities and insurance premiums for officers

ARPC has entered into a deed of indemnity with each of its Members. The indemnity is consistent with the requirements of the *Commonwealth Authorities and Companies Act 1997* in relation to such indemnities.

During the year, ARPC maintained and paid premiums for insurance covering Members and certain employees. The premium paid for the insurance, which includes liability for legal costs, was $67,566.43 (2006: $ $26,691.58).*

Judicial and administrative decisions and reviews

During the year ended 30 June 2007, there were no judicial decisions or reviews by outside bodies (other than ANAO's report on the financial statements) affecting ARPC of which it is aware.

Ecologically sustainable development

ARPC implements strategies designed to minimise waste and conserve energy.

ARPC recycles paper products, cardboard products and used toner cartridges.

---

* The difference in premium is explained by the fact that a decision was taken in 2005-06 to align the expiry dates of all ARPC's insurance policies to 30 June in each year. Consequently, the premium paid in 2005-06 was for the period 12 March 2006 to 30 June 2006.

Freedom of information

There were no freedom of information requests during the year ended 30 June 2007. The following statements are made as required by section 8 of the *Freedom of Information Act 1982*.

Functions, organisation and powers

ARPC's functions and powers are detailed in Chapter 1. An organisation chart is contained in Appendix 1.

Arrangements for outside participation

People or organisations outside ARPC may participate in policy formulation or the administration of its enactments by making representations to the Treasurer or to ARPC.

In addition, employees of ARPC meet regularly with industry bodies, clients and other interested parties outside the Australian Government for discussions on various matters.

ARPC documents and publications

ARPC produces a number of publications aimed at informing clients and others of ARPC and its functions. Key publications in 2006-07 included:

- 2005-06 Annual Report;
- a paper entitled *Financial Management of Catastrophes in Australia* by Neil Weeks — this paper formed the basis of Mr Weeks' presentation to the OECD International Network on the Financial Management of Large-scale Catastrophes held in Hyderabad, India on 26-27 February 2007;
- Terrorism Insurance Scheme — a brochure outlining the basis of the scheme;
- a brochure of frequently asked questions; and
- *Under the Cover* — a quarterly electronic newsletter distributed to clients and other stakeholders.

Facilities for access

Facilities for inspecting documents are provided at ARPC's head office at:

Level 2 London Court
13 London Circuit
CANBERRA ACT 2600

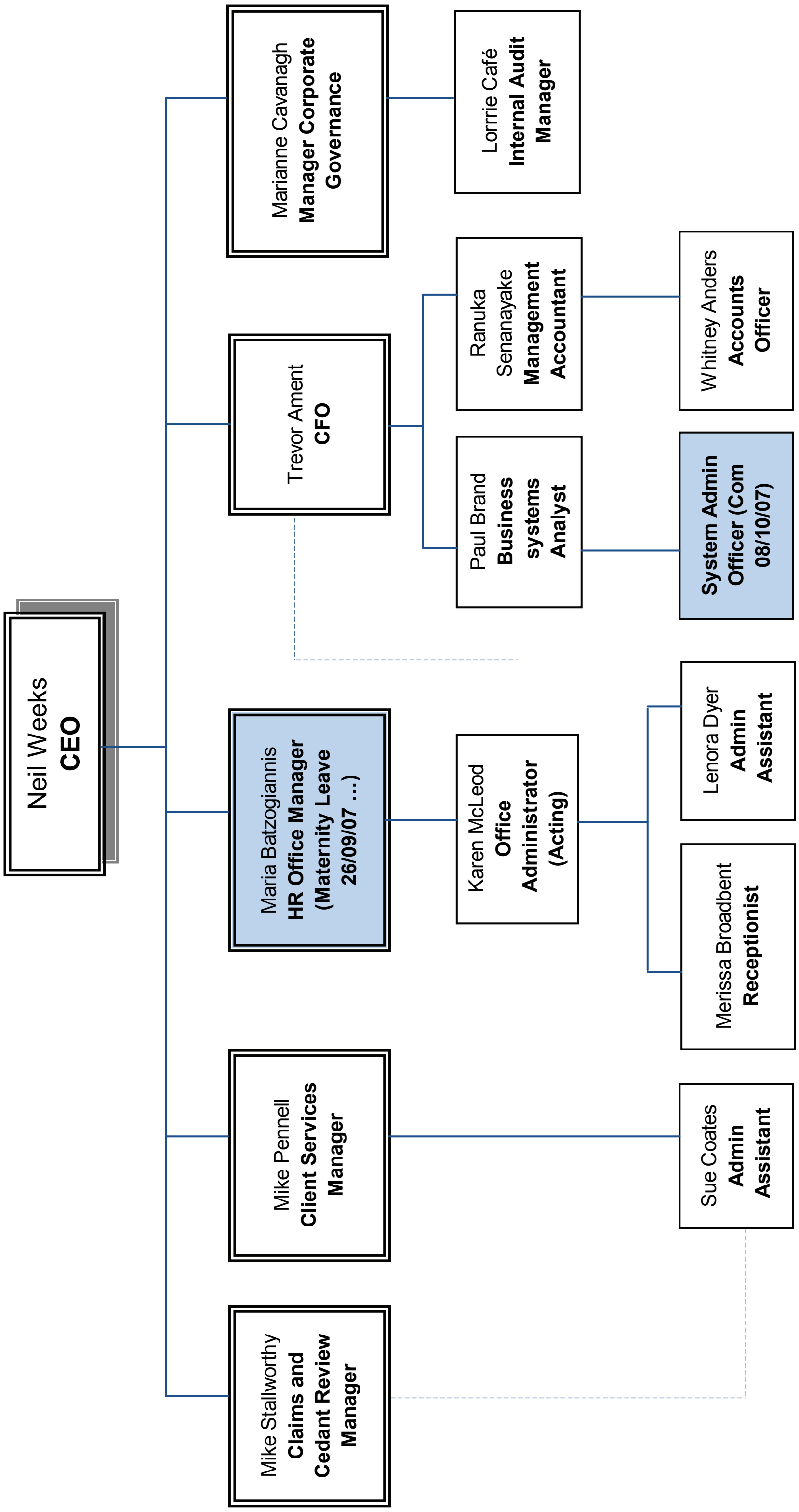
Access may also be given at our Sydney office by prior arrangement.

Freedom of information procedures and initial contact point

Inquiries concerning access to documents or other matters relating to freedom of information should be directed to:

Chief Executive
Australian Reinsurance Pool Corporation
GPO Box 3024
CANBERRA ACT 2601
Tel: 02 6279 2100
Fax: 02 6279 2111

Appendix A


Neil Weeks
CEO
Marianne Cavanagh
Manager Corporate Governance
Lorrie Café
Internal Audit Manager
Trevor Ament
CFO
Ranuka Senanayake
Management Accountant
Whitney Anders
Accounts Officer
Paul Brand
Business systems Analyst
System Admin Officer (Com 08/10/07)
Maria Batzogiannis
HR Office Manager
(Maternity Leave 26/09/07 ...)
Karen McLeod
Office Administrator (Acting)
Lenora Dyer
Admin Assistant
Merissa Broadbent
Receptionist
Mike Pennell
Client Services Manager
Sue Coates
Admin Assistant
Mike Stallworthy
Claims and Cedant Review Manager

Appendix B

THE HONOURABLE CHRIS PEARCE MP
Parliamentary Secretary to the Treasurer
Federal Member for Aston

Mr J I Gersh AM
Chairman
Australian Reinsurance Pool Corporation
GPO Box 3024
CANBERRA ACT 2601

– 3 MAY 2007

Dear Mr Gersh

I am pleased to provide you with the Australian Government's Statement of Expectations for the Australian Reinsurance Pool Corporation. This Statement forms part of the implementation of the Government's response to the *Review of Corporate Governance of Statutory Authorities and Office Holders*, which was conducted by Mr John Uhrig AC (the Uhrig Report). The Uhrig Report identified ways in which the governance of Commonwealth portfolio bodies may be improved and recommended options for increasing transparency and accountability and ensuring well-defined responsibilities and clear relationships between portfolio bodies and other arms of Government.

The Government is issuing a Statement of Expectations to portfolio bodies and requesting that portfolio bodies respond with a Statement of Intent. The Government looks forward to receiving the ARPC's Statement of Intent within three months of the date of this letter. In the interest of public accountability, both of these documents will be made public. This Statement will be reviewed as circumstances require.

This Statement of Expectations outlines the Government's current expectations with regard to the role and responsibilities of the ARPC, the ARPC's relationships with the Government, issues of transparency and accountability, and operational issues.

At the outset, I would like to make it clear that the Government is very pleased with the overall performance of the ARPC as the administrator of the terrorism insurance scheme. The *Review of the Terrorism Insurance Act: 2006* conducted by the Treasury found the ARPC to be efficient and prudent.

The role and responsibilities of the ARPC

The Government established a scheme through the *Terrorism Insurance Act 2003* (the Act) to provide terrorism insurance coverage for commercial property and associated business interruption and public liability cover. The scheme, which commenced on 1 July 2003, was developed following the progressive withdrawal of commercial terrorism insurance cover in the aftermath of the terrorist attacks in the United States of America on 11 September 2001.

If the Minister declares a terrorist incident, the Act overrides terrorism exclusion clauses in eligible insurance contracts and insurers are then required to cover eligible terrorism losses. The Government established the ARPC to provide reinsurance cover for this risk. Insurance companies are able, although not compelled, to reinsure this risk with the ARPC. Consistent with industry practice, the ARPC charges insurers premiums for this reinsurance; premiums are set by ministerial determination.

Suite 4, Level 1, 420 Burwood Highway, Wantirna South VIC 3152 • Telephone 03 9887 3890 Facsimile 03 9887 3893

In addition to this primary role of providing terrorism reinsurance, the ARPC should seek to be in a position to advise the responsible Treasury minister of likely costs to the ARPC in the event of a declared terrorist incident. To this end, the ARPC should model different scenarios to estimate the potential exposure if a terrorist incident occurs.

The Act, and the scheme it establishes, is intended to be in place in the short term, until sufficient terrorism insurance is available on reasonable terms. In keeping with this objective, the ARPC should also seek to keep abreast of key international developments including other government-run schemes and the affordability and availability of commercial terrorism insurance. The ARPC should inform Treasury and the Government of any key developments.

Relationships of the Board

Relationship with the Minister

I expect that the ARPC will keep the Government fully informed of its activities, and will alert the Government of any significant events related to the ARPC's core business in a timely manner. Accurate and timely advice to the responsible Treasury minister is essential to ensure the Government is best placed to respond promptly to matters that might arise.

Relationship with the Treasury

The role of the Treasury is to support and advise me and other Treasury ministers in our responsibilities by being the principal source of advice on a wide range of issues, including policy development and the review of results. The ARPC is primarily responsible for the administration of the terrorism insurance scheme.

To fulfil these respective roles in the area of terrorism insurance, the Treasury and the ARPC should maintain a close working relationship. The Treasury takes into account the views and experience of the ARPC when considering and advising on changes to terrorism insurance policy and legislation. By advising the Treasury on the operational implications of Government policy initiatives, the ARPC contributes to policy development. It is also imperative that the ARPC continues to consult with the Treasury in the development of substantive operational policies to facilitate consistency between the objectives of legislation and its practical implementation.

The Government accepted the Uhrig Report recommendation that portfolio bodies should provide information to portfolio secretaries in parallel to that information being provided to ministers. The ARPC should keep the Secretary to the Treasury appropriately informed of significant high-level meetings between the ARPC and Government ministers and other key policy figures. This should ensure that the Treasury continues to be placed in a good position to fulfil its role as the principal source of advice on terrorism insurance policy matters to the Government. The Chair of the ARPC, together with the other members of the Board, remains responsible for the direct oversight of the ARPC.

Relationship with clients

The ARPC interacts directly with its clients, that is, those insurers that reinsure their terrorism risk with the ARPC.

It is important for insurers to be aware of their exposure under the Act. The ARPC should seek to continue to educate all insurers covered by the Act, both in Australia and overseas, about its objectives and its implications.

Transparency and accountability

The ARPC was established as an independent body to administer the terrorism insurance scheme. However, the ARPC performs its statutory functions as part of the Australian Government and remains accountable to the Parliament, and ultimately to the public, through the Treasury ministers, the Parliamentary Committee process and the tabling of its annual report. Open consultation and a sound working relationship with its clients should help to ensure that the ARPC interacts with market participants and the community more generally in a transparent and accountable manner.

In keeping with corporate governance best practice, the Board should conduct annual self-assessments. Evaluation helps boards do their job more effectively. The Board's self-assessment should look at the performance of the Board as a whole as well as focusing on the performance of individual members. The Uhrig Report noted that having an independent person, who is appropriately qualified, examine and report on the assessment is the most effective mechanism of providing accurate feedback. I recommend this approach to you but I understand that there are costs involved and it may not be the most appropriate approach for the ARPC every year.

The Chair will meet with the responsible Treasury minister at least annually and discuss the performance of the Board. The Chair should be in a position to discuss the outcome of the annual performance evaluation of the Board and the performance of specific directors.

Operational issues

I expect that the ARPC will maintain the highest standards of corporate governance, and implement policies and strategies to ensure that the ARPC's officers adhere to the ARPC's code of conduct at all times.

The requirements for the ARPC's financial management are set out in the relevant legislative requirements and the Finance Minister's Orders. In this regard, I note that it is the intention of the Government that the ARPC remain an agency prescribed under the *Commonwealth Authorities and Companies Act 1997*.

It is Government policy that all departments and portfolio bodies should continue efforts to secure improved efficiency in their operations and demonstrate value for money for the services that they deliver. I appreciate that the ARPC continues to seek opportunities to achieve outcomes in a more cost-effective manner.

The review of the Act

The Act stipulates a review must occur at least once every three years after the scheme commences. The Treasurer must prepare a report that reviews the need for the Act to continue in operation. The ARPC is expected to contribute to the review process, providing information, advice and expertise.

Conclusion

The Government's vision is that ARPC remains a high performing and responsive advisory body that continues to be the administrator of the terrorism insurance scheme. I look forward to working with the ARPC under the new governance arrangements.

I have copied this correspondence to the Treasurer, the Prime Minister and the Minister for Finance and Administration.

Yours sincerely

CHRIS PEARCE

Appendix C

Australian Government

Australian Reinsurance Pool Corporation

24 July 2007

File: REV54G

The Hon Chris Pearce MP
Parliamentary Secretary to the Treasurer
Parliament House
Canberra ACT 2600

Dear Mr Pearce

Statement of Intent

Thank you for your letter of 3 May 2007 in which you set out the Australian Government's expectations of the Australian Reinsurance Pool Corporation with regard to the role and responsibilities of ARPC, ARPC's relationships with the Government, issues of transparency and accountability and operational issues.

I am pleased to respond to the Government's Statement of Expectations with ARPC's Statement of Intent.

The role and responsibilities of ARPC

ARPC recognises that its role is to administer the scheme established under the *Terrorism Insurance Act 2003* to provide terrorism insurance coverage for commercial property and associated business interruption and public liability cover.

The scheme requires ARPC to offer terrorism reinsurance to insurers which write eligible insurance contracts. The premiums charged for the reinsurance offered by ARPC are set by Ministerial Direction.

In addition to its primary role of providing terrorism reinsurance, ARPC will seek to be in a position to advise the responsible Treasury minister of likely costs to ARPC in the event that a declared terrorist incident is announced under the Act. ARPC has a number of strategies in place to enable it to meet this expectation.

Annual aggregate reports

The standard reinsurance agreement obliges each cedant to provide ARPC with an annual aggregate report. The report summarises the cedant's aggregate exposures to building, contents and business interruption risks at post code level. This information allows ARPC to analyse the distribution of exposure risk across Australia.

Correspondence to: GPO Box 3024, CANBERRA ACT 2601
13 London Circuit, CANBERRA ACT 2600
Telephone: (02) 6279 2100 Facsimile: (02) 6279 2111 Email: arpc@treasury.gov.au
ABN 74807136872
www.arpc.gov.au

Loss estimation models

ARPC has undertaken considerable work towards developing loss estimation models which will enable it to estimate its potential exposure in the event of a declared terrorist incident. ARPC will continue to develop these models and will test the models using various disaster scenarios. ARPC will also foster alliances with industry bodies and other agencies which are undertaking similar work.

ARPC seeks to keep abreast of key international developments. To this end, ARPC monitors insurance journals and other industry publications, meets regularly with insurers and reinsurers which have international experience and presence and maintains contact with representatives of various overseas reinsurance pools.

One particular contact which adds significantly to ARPC's ability to monitor international developments is the CEO's membership of the Advisory Board to the OECD Network on the Financial Management of Large-scale Catastrophes. Membership of the Advisory Board includes the United Kingdom, France, Spain, China and the United States of America and several other developing nations. It also includes representatives of academic institutions and private sector organisations. This gives the CEO insights into current trends in catastrophe management. The CEO also attends Network conferences which attract delegates from most OECD member countries and provide opportunities to consider developments in industry and government responses to large-scale catastrophes.

Relationships of the Board

Relationship with the Minister

ARPC recognises that accurate and timely advice to the responsible Treasury ministers is essential to ensure the Government is best placed to respond promptly to matters that might arise. ARPC will keep the Government fully informed of its activities, and will alert the government in a timely manner to any significant events related to ARPC's core business.

Relationship with the Treasury

ARPC recognises that Treasury is the principal source of advice to Treasury ministers on a wide range of issues, including policy development and the review of results. ARPC will maintain a close working relationship with Treasury, including holding quarterly meetings between the Treasury policy officers responsible for terrorism insurance and ARPC management. ARPC will advise Treasury on the operational implications of government policy initiatives. It will also consult with Treasury in the development of substantive operational policies to facilitate consistency between the objectives of the legislation and its practical implementation.

ARPC will keep the Secretary to the Treasury appropriately informed of significant high-level meetings between ARPC and Government ministers and other key policy figures.

Relationship with clients

ARPC seeks to ensure that all issuers of eligible insurance contracts are aware of their exposure to eligible terrorism losses by virtue of the operation of the Act. The public speaking program conducted by senior management, direct contact with clients and potential clients and the maintenance of appropriate industry contacts, including regular visits to the major insurance centres, is designed to ensure that all insurers covered by the Act, both in Australia and overseas, are aware of its objectives and its implications.

Transparency and accountability

ARPC is a Commonwealth authority as defined in the *Commonwealth Authorities and Companies Act 1997*. Under that Act, ARPC must report to the responsible Minister and, through that reporting process, to the Parliament and, ultimately, to the public.

To assist ARPC to interact with market participants and the community more generally in a transparent and accountable manner, ARPC will continue to maintain open consultation and sound working relationships with its clients.

The Board's performance is evaluated annually. This is usually conducted by means of a self-assessment undertaken by each Board member and looks at the performance of the Board as a whole as well as the performance of the individual member. The results of the self-assessments are forwarded to the Chair for review and discussed by members at the following Board meeting. For the review conducted in 2005-06 ARPC engaged the services of an independent consultant to examine and report on the assessment and will do so again when the members consider this approach to be appropriate.

The Chair will meet with the responsible Treasury minister as least annually. At this meeting the Chair will be in a position to discuss the outcome of the annual performance evaluation of the Board and the performance of specific directors.

Operational issues

ARPC will maintain the highest standard of corporate governance and implement policies and strategies to ensure that ARPC's officers adhere to ARPC's code of conduct at all times. ARPC's mission, objectives, values and code of conduct are published in its business plan each year and are also displayed prominently in its offices. The code of conduct is promulgated by management at staff meetings.

ARPC notes that it is to remain a Commonwealth agency under the *Commonwealth Authorities and Companies Act 1997*. It will continue to comply with its obligations under that Act and the obligations imposed by the Finance Minister's orders made in accordance with that Act.

ARPC will continue to seek opportunities to achieve outcomes in the most cost-effective manner in order to secure improved efficiency in its operations and obtain value for money.

The review of the Act

ARPC notes that the scheme must be reviewed at least once every three years after commencement. ARPC will contribute to the review process by providing information, advice and expertise.

4

Conclusion

ARPC is pleased to note that the Government considers that ARPC is a high performing and responsive advisory body and it will seek to remain so. ARPC looks forward to working under the new governance arrangements in continuing to administer the terrorism insurance scheme.

Yours sincerely

J I Gersh
Chairman

Chapter 5: Financial statements

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Statement by Members and Chief Executive

In our opinion, the attached financial statements for the year ended 30 June 2007 have been prepared based on properly maintained financial records and give a true and fair view of the matters required by the Finance Minister's Orders made under the *Commonwealth Authorities and Companies Act 1997*.

In our opinion, at the date of this statement, there are reasonable grounds to believe that the Australian Reinsurance Pool Corporation will be able to pay its debts as and when they become due and payable.

This statement is made in accordance with a resolution of the Members.

J I Gersh
Chair
11 September 2007

N E Weeks
Chief Executive
11 September 2007

T R Ament
Chief Financial Officer
11 September 2007

Australian National
Audit Office

INDEPENDENT AUDITOR'S REPORT

To the Treasurer

Scope

I have audited the accompanying financial statements of the Australian Reinsurance Pool Corporation for the year ended 30 June 2007, which comprise: a statement by Members and Chief Executive; income statement; balance sheet; statement of changes in equity; cash flow statement; schedules of commitments and contingencies; a summary of significant accounting policies; and other explanatory notes.

The Responsibility of Members for the Financial Statements

The members of the Australian Reinsurance Pool Corporation are responsible for the preparation and fair presentation of the financial statements in accordance with the Finance Minister's Orders made under the *Commonwealth Authorities and Companies Act 1997* and the Australian Accounting Standards (including the Australian Accounting Interpretations). This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

My responsibility is to express an opinion on the financial statements based on my audit. My audit has been conducted in accordance with the Australian National Audit Office Auditing Standards, which incorporate the Australian Auditing Standards. These Auditing Standards require that I comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor

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19 National Circuit BARTON ACT
Phone (02) 6203 7300 Fax (02) 6203 7777

considers internal control relevant to the Authority's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Members of the Australian Reinsurance Pool Corporation, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Independence

In conducting the audit, I have followed the independence requirements of the Australian National Audit Office, which incorporate the ethical requirements of the Australian accounting profession.

Auditor's Opinion

In my opinion, the financial statements of the Australian Reinsurance Pool Corporation:

(a) have been prepared in accordance with the Finance Minister's Orders made under the *Commonwealth Authorities and Companies Act 1997,* and the Australian Accounting Standards (including the Australian Accounting Interpretations); and

(b) give a true and fair view of the matters required by the Finance Minister's Orders including the Australian Reinsurance Pool Corporation's financial position as at 30 June 2007 and of its financial performance and its cash flows for the year then ended.

Australian National Audit Office

11 September 2007

Warren Cochrane
Group Executive Director

Delegate of the Auditor-General

Canberra

Income statement

for the period ended 30 June 2007

	Notes	2007 $'000	2006 $'000
Premium revenue	4(a)	**96,890**	102,537
Outwards reinsurance expense		**-**	-
Net premium revenue		**96,890**	102,537
Claims expense		**-**	-
Reinsurance and other recoveries revenue		**-**	-
Net claims incurred		**-**	-
Acquisition costs	5(b)	**(412)**	(930)
Underwriting result		**96,478**	101,607
Investment income	4(b)	**18,803**	10,833
Other income	4(c)	**5**	15
Other operating expenses	5(b)	**(3,973)**	(3,034)
Operating result		**111,313**	109,421

The above statement should be read in conjunction with the accompanying notes.

Balance sheet
as at 30 June 2007

	Notes	2007 $'000	2006 $'000
Current assets			
Cash and cash equivalents	6	**91,508**	67,254
Receivables	7	**23,492**	25,213
Investments	8	**263,000**	187,867
Deferred acquisition costs	9	**392**	820
Other non-financial assets	10	**27**	31
Total current assets		**378,419**	281,185
Non-current assets			
Property plant and equipment	11(c)	**338**	427
Intangibles	11(d)	**171**	85
Total non-current assets		**509**	512
Total assets		**378,928**	281,697
Current liabilities			
Unearned premium liability	12	**46,189**	48,350
Payables	13	**434**	12,389
Other interest bearing liabilities	14	**6**	13
Employee provisions	15(a)	**139**	133
Total current liabilities		**46,768**	60,885
Non-current liabilities			
Other interest bearing liabilities	14	**-**	6
Employee provisions	15(a)	**101**	68
Other provisions	15(b)	**49**	41
Total non-current liabilities		**150**	115
Total liabilities		**46,918**	61,000
Net assets		**332,010**	220,697
Equity			
Accumulated reserves		**-**	-
Reserve for claims		**332,010**	220,697
Total equity		**332,010**	220,697

The above statement should be read in conjunction with the accompanying notes.

Cash flow statement

for the year ended 30 June 2007

	Notes	2007 $'000	2006 $'000
Operating activities			
Cash received			
Premiums received		**105,327**	112,161
Interest received		**18,589**	10,257
Total cash received		**123,916**	122,418
Cash used			
Creditors and employees		**3,658**	4,043
Interest and other costs of finance paid		**248**	252
Net goods and services tax paid to ATO		**8,471**	9,180
Total cash used		**12,377**	13,475
Net cash from or (used by) operating activities		**111,539**	108,943
Investing activities			
Cash used			
Purchase of plant and equipment		**19**	326
Purchase of intangibles		**112**	20
Purchase of investments		**87,154**	75,854
Total cash used		**87,285**	76,200
Net cash from or (used by) investing activities		**(87,285)**	(76,200)
Net increase or (decrease) in cash held		**24,254**	32,743
Cash at the beginning of the reporting period		**67,254**	34,511
Cash at the end of the reporting period	6	**91,508**	67,254

The above statement should be read in conjunction with the accompanying notes.

Statement of changes in equity
as at 30 June 2007

	Notes	Accumulated results		Reserve for claims		Total equity	
		2007	2006	**2007**	2006	**2007**	2006
		$'000	$'000	**$'000**	$'000	**$'000**	$'000
Opening balance		**-**	-	**220,697**	111,276	**220,697**	111,276
Income and expenses							
Net operating result		**111,313**	109,421	-	-	**111,313**	109,421
Total income and expenses		**111,313**	109,421	**-**	-	**111,313**	109,421
Transfers between equity components							
Transfer to reserve for claims	1(m)	**(111,313)**	(109,421)			**(111,313)**	(109,421)
Transfer to reserve for claims from accumulated results				**111,313**	109,421	**111,313**	109,421
Closing balance at 30 June		**-**	**-**	**332,010**	220,697	**332,010**	220,697

The above statement should be read in conjunction with the accompanying notes.

Schedule of commitments
as at 30 June 2007

	2007 $'000	2006 $'000
By type		
Other commitments		
Service level agreements *	**284**	474
Software license agreement**	**30**	60
Software development agreement***	**404**	-
Operating leases ****	**109**	326
Total other commitments	**827**	860
Commitments receivable	**75**	78
Net commitments by type	**752**	782
By maturity		
Service level agreements commitments		
One year or less	**284**	284
From one to five years	**-**	190
Total service level agreements commitments	**284**	474
Software licence agreement commitments		
One year or less	**30**	30
From one to five years	**-**	30
Total software licence agreement commitments	**30**	60
Software development agreement commitments		
One year or less	**404**	-
From one to five years	**-**	-
Total software development agreement commitments	**404**	-
Operating lease commitments		
One year or less	**109**	217
From one to five years	**-**	109
Total operating lease commitments	**109**	326
Commitments receivable	**75**	78
Net commitments by maturity	**752**	782

NB: Commitments are GST inclusive where relevant.

* Outstanding contractual payments for service level agreements.

** Outstanding contractual payments for software licence agreement.

*** Outstanding contractual payments for software develpoment agreement.

**** Operating leases included are effectively non-cancellable and comprise:

Nature of lease	*General description of leasing agreement*
Lease for office accommodation	Upon exercising the 3 year lease option the rent will be reviewed in accordance with prevailing market conditions.

Schedule of contingencies
as at 30 June 2007

ARPC has no contingent assets or liabilities

The above schedules should be read in conjunction with the accompanying notes.

Notes to and forming part of the financial statements for the year ended 30 June 2007

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Note 1: Summary of significant accounting policies

ARPC is a statutory authority that was established as an independent entity wholly owned by the Commonwealth of Australia (Commonwealth) on 1 July 2003 by the *Terrorism Insurance Act 2003* (TI Act).

The TI Act effectively deems terrorism risk cover into eligible insurance contracts by rendering terrorism exclusions void. Insurance companies may reinsure this additional risk with ARPC.

ARPC has the power to do all things necessary in connection with the performance of its functions.

The following accounting policies have been adopted in the financial statements.

(a) Basis of preparation of the financial statements

The financial statements and notes are required by clause 1(b) of Schedule 1 to the *Commonwealth Authorities and Companies Act 1997* and are a general purpose financial report.

The continued existence of ARPC in its present form and with its present programs is dependent on Government policy.

The financial statements and notes have been prepared in accordance with:

- Finance Minister's Orders (FMOs) for reporting periods ending on or after 1 July 2006; and
- Australian Accounting Standards and interpretations issued by the Australian Accounting Standards Board (AASB) that apply for the reporting period.

The financial statements have been prepared on an accrual basis and are in accordance with historical cost convention, except for certain assets and liabilities which, as noted, are at fair value. Except where stated, no allowance is made for the effect of changing prices on the results or the financial position.

The financial statements are presented in Australian dollars and values are rounded to the nearest thousand dollars unless disclosure of the full amount is specifically required (Note 1(y)).

Unless alternative treatment is specifically required by an Accounting Standard or the FMOs, assets and liabilities are recognised in the Balance Sheet when and only when it is probable that future economic benefits will flow to ARPC and the amounts of the assets or liabilities can be reliably measured. However, assets and liabilities arising under agreements equally proportionately unperformed are not recognised unless required by an Accounting Standard. Liabilities and assets that are unrealised are reported in the Schedule of Commitments and the Schedule of Contingencies (Note 22).

Unless alternative treatment is specifically required by an accounting standard, revenues and expenses are recognised in the Income Statement when and only when the flow, consumption or loss of economic benefits has occurred and can be reliably measured.

(b) Going concern

These financial statements have been prepared on the basis that ARPC is a going concern.

(c) Significant accounting judgements and estimates

In the process of applying the accounting policies listed in this note, ARPC has made the following estimate based on historical experience and other factors that have the most significant impact on the amounts recorded in the financial statements:

- the unclosed business estimate required by note 1(e) for premium revenue was based on the previous year's actual unclosed business with due allowance made for any changes in the pattern of new business and renewals.

No accounting assumptions or estimates have been identified that have a significant risk of causing a material adjustment to carrying amounts of assets and liabilities within the next accounting period.

(d) Statement of compliance

Australian Accounting Standards require a statement of compliance with International Financial Reporting Standards (IFRSs) to be made where the financial report complies with these standards. Some Australian equivalents to IFRSs and other Australian Accounting Standards contain requirements specific to not-for-profit entities that are inconsistent with IFRS requirements. ARPC is a not-for-profit entity and has applied these requirements, so while the financial statements comply with Australian Accounting Standards including Australian Equivalents to International Reporting Standards (AEIFRSs) it cannot make this statement.

Adoption of new Australian Accounting Standard requirements

No accounting standard has been adopted earlier than the effective date in this current period.

ARPC is required to disclose Australian Accounting Standards and Interpretations which have been issued but are not yet effective that have not been early adopted by ARPC. The following amendments, revised standards or interpretations have become effective but have had no financial impact or do not apply to the operations of ARPC.

Amendments:

- 2005-4 amendments to Australian Accounting Standards [AASB 139, AASB 132, AASB 1, AASB 1023 and AASB 1038];
- 2005-5 amendments to Australian Accounting Standards [AASB 1 and AASB 139];
- 2005-9 amendments to Australian Accounting Standards [AASB 4, AASB 1023, AASB 139 and AASB 132];
- 2005–1 amendments to Australian Accounting Standards [AASBs 1, 101, 124];
- 2005–6 amendments to Australian Accounting Standards [AASB 3];
- 2006–1 amendments to Australian Accounting Standards [AASB 121]; and
- 2006–3 amendments to Australian Accounting Standards [AASB 1045].

Interpretations:

- UIG 4 Determining whether an arrangement contains a Lease;
- UIG 5 Rights to Interests arising from Decommissioning, Restoration and Environment Rehabilitation Funds;
- UIG 7 Applying the Restatement Approach under AASB 129 Financial Reporting in Hyperinflationary Economies;
- UIG 8 Scope of AASB 2; and
- UIG 9 Reassessment of Embedded Derivatives.

UIG 4 and UIG 9 might have impacts in future periods, subject to existing contracts being renegotiated.

Future Australian Accounting Standard requirements

The following new standards, amendments to standards or interpretations have been issued by the Australian Accounting Standards Board but are effective for future reporting periods. It is estimated that the impact of adopting these pronouncements when effective will have no material financial impact on future reporting periods.

Financial instrument disclosure

AASB 7 Financial Instruments: Disclosure is effective for reporting periods beginning on or after 1 January 2007 (the 2007–08 financial year) and amends the disclosure requirements for financial instruments. In general AASB 7 requires greater disclosure than that presently required. Associated with the introduction of AASB 7 a number of accounting standards were amended to reference the new standard or remove the present disclosure requirements through 2005 — 10 Amendments to Australian Accounting Standards [AASB 132, AASB 101, AASB 114, AASB 117, AASB 133, AASB 139, AASB 1, AASB 4, AASB 1023 and AASB 1038]. These changes have no financial impact but will affect the disclosure presented in future financial reports.

Other

The following standards and interpretations have been issued but are not applicable to the operations of ARPC.

- AASB 1049 Financial Reporting of General Government Sectors by Governments; and
- UIG 10 Interim Financial Reporting and Impairment.

(e) Revenue

Premium revenue

Premium revenue comprises amounts charged to insurers excluding taxes collected on behalf of third parties. The earned portion of premiums received and receivable, including unclosed business, is recognised as revenue in the Income Statement. Premiums are recognised as earned based on time from the date of attachment of risk. Premiums not received at reporting date and for the quarter ended 30 June 2007 are recognised as premiums receivable in the Balance Sheet.

The proportion of premium received or receivable not earned in the Income Statement at the reporting date is recognised in the Balance Sheet as unearned premium.

Unearned premiums are determined using the eighth system, a fractional method of calculation of the balance. This method is driven by the assumption that the risk attached to the revenue ceded expires evenly over each quarter of the financial year.

Premiums on unclosed business are brought to account using estimates based on the previous year's actual unclosed business with due allowance made for any changes in the pattern of new business and renewals.

Investment revenue

Interest revenue is recognised using the effective interest method as set out in AASB 139.

(f) Unexpired risk liability

ARPC has compared the net present value of the expected future cash flows relating to future claims arising under general insurance contracts with the reported unearned premium liability.

There is no deficiency noted or recorded in these financial statements (2006: $0). Accordingly, there has been no write down in ARPC's deferred acquisition costs.

(g) Outstanding claims liability

The financial statements have not included a provision for outstanding claims (2006: $0). ARPC has not engaged an actuarial assessment to independently assess this balance as:

- a declared terrorist incident has not been announced since the inception of ARPC; and
- any such declaration must be announced by the Treasurer after consultation with the Attorney-General.

ARPC considers that there are no significant inherent uncertainties in respect of the liability estimate. Accordingly, ARPC has not applied a central estimate to the provision and has not, therefore, applied a prudential or safety margin in respect of the provision.

(h) Net claims incurred

A declared terrorist incident has not been announced since the inception of ARPC.

(i) Assets backing general insurance liabilities

With the exception of property plant and equipment and intangibles, ARPC has determined that all assets are held to back general insurance liabilities and their accounting treatment is described below.

Financial assets

Financial assets are designated at fair value through the Income Statement. Initial recognition is at cost in the Balance Sheet and subsequent measurement is at fair value with any resultant unrealised profits and losses recognised in the Income Statement.

Details of fair value for the different types of financial assets are listed below

Cash

- Cash assets are carried at face value of the amounts deposited or drawn. The carrying amounts of cash assets are approximate to their fair value. For the purposes of the Statement of Cash Flows, cash includes cash on hand and deposits held at call with banks.

Investments

- Fixed interest deposits are carried at face value of the amounts deposited. The carrying amounts are approximate to their fair value.

- Government (guaranteed) securities are initially recognised at cost and the subsequent fair value is taken as the quoted bid price of the security at the Balance Sheet date. All Government securities are classified as available for sale.

All purchases and sales of financial assets that require delivery of the asset with the time frame established by regulation or market convention are recognised at trade date, being the date on which ARPC commits to buy or sell the asset.

In cases where the period between trade and settlement exceeds the time frame, the transaction is recognised at settlement date. Financial assets are derecognised when the rights to receive future cash flows from the assets have expired, or have been transferred, and ARPC has transferred substantially all the risks and rewards of ownership.

Receivables

Amounts due from policyholders and intermediaries are held for trading and are initially recognised at fair value, being the amounts due. They are subsequently measured at fair value which is approximated by taking the initially recognised amount and reducing it for impairment as appropriate.

A provision for impairment of receivables is established when there is objective evidence that ARPC will not be able to collect all amounts due according to the original terms of the receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows. The discount is calculated using a risk free rate. The impairment charge is recognised in the Income Statement.

(j) Impairment of financial assets

Financial assets are assessed for impairment at each balance date.

Financial assets held at amortised cost

If there is objective evidence that an impairment loss has been incurred for receivables, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The carrying amount is reduced by way of an allowance account. The loss is recognised in the Income Statement.

Available for sale financial assets

If there is objective evidence that an impairment loss on an available for sale financial asset has been incurred, the amount of the difference between its cost, less principal repayments and amortisation, and its current fair value, less any impairment loss previously recognised in expenses, is transferred from equity to the Income Statement.

(k) Deferred acquisition costs

Acquisition costs are incurred in obtaining and recording policies of insurance. They include legal, advertising, risk assessment and other administrative costs.

A portion of acquisition costs relating to unearned premium revenue is deferred in recognition that it represents future benefits to the organisation where they can be reliably measured and where it is probable that they will give rise to premium revenue that will be recognised in the Income Statement in subsequent reporting periods. Deferred acquisition costs are measured at the lower of cost and recoverable amount. These costs are amortised on the same basis as the earning pattern of the corresponding premium revenue.

(l) Dividends

Pursuant to section 38(3)(b) of the TI Act, the Minister may give written direction to require ARPC to make payments to the Commonwealth in the nature of dividends. No direction has been received for these financial statements (2006: $0).

(m) Reserves

The intention of the Government in establishing ARPC was that premiums would be used to fund a pool and to repay any loan required in the event that claims exceed the resources of the pool. The reserve for claims has been created to enable ARPC to build up the required pool.

(n) Foreign currency

All foreign transactions are converted to Australian dollars at the exchange rate at the date of the transaction. There has been no foreign currency transactions recognised in the financial statements (2006: $0).

(o) Employee benefits

Liabilities for services rendered by employees are recognised at the reporting date to the extent that they have not been settled.

Liabilities for 'short-term employee benefits' (as defined in AASB 119) and termination benefits due within twelve months of balance date are measured at their nominal amounts.

The nominal amount is calculated with regard to the rates expected to be paid on settlement of the liability.

All other employee benefit liabilities are measured as the present value of the estimated future cash outflows to be made in respect of services provided by employees up to the reporting date.

Leave

The liability for employee benefits includes provision for annual leave and long service leave. No provision has been made for sick leave as all sick leave is non-vesting and the average sick leave taken in future years by employees of ARPC is estimated to be less than the annual entitlement for sick leave.

The leave liabilities are calculated on the basis of employees' remuneration, including ARPC's employer superannuation contribution rates to the extent that the leave is likely to be taken during service rather than being paid out on termination.

The liability for long service leave has been determined by reference to the work of an actuary as at 30 June 2006. The estimate of the present value of the liability takes into account attrition rates and pay increases through promotion and inflation.

Superannuation

Superannuation guarantee contributions are made by ARPC for employees and certain Members.

The Australian Workplace Agreements between ARPC and its employees allow for choice of superannuation fund. The default superannuation scheme is the Australian Government Employees Superannuation Trust.

The liability for superannuation recognised as at 30 June represents outstanding contributions for the final fortnight of the year.

(p) Leases

A distinction is made between finance leases and operating leases. Finance leases effectively transfer from the lessor to the lessee substantially all the risks and rewards incidental to ownership of leased non-current assets. An operating lease is a lease that is not a finance lease. In operating leases, the lessor effectively retains substantially all such risks and benefits.

ARPC entered into an operating lease agreement for office accommodation. Operating lease payments are expensed on a straight line basis which is representative of the pattern of benefits derived from the leased assets.

(q) Financial risk management

ARPC's activities expose it to normal commercial financial risks. As a result of the nature of ARPC's business and internal and Australian Government policies, dealing with the management of financial risk, ARPC's exposure to credit, liquidity and cash flow and fair value interest rate risk is considered to be low.

(r) Derecognition of financial assets and liabilities

Financial assets are derecognised when the contractual rights to the cash flows from the financial assets expire or the asset is transferred to another entity. In the case of a transfer to another entity, it is necessary that the risks and rewards of ownership are also transferred.

Financial liabilities are derecognised when the obligation under the contract is discharged, cancelled or expires.

No financial assets or liabilities were derecognised in these financial statements (2006: $0).

(s) Trade creditors

ARPC's trade creditors and accruals are recognised at their nominal amounts, being the amounts at which the liabilities will be settled. Liabilities are recognised to the extent that the goods or services have been received (irrespective of having been invoiced).

All payables are unsecured and are paid within credit terms.

(t) Contingent liabilities and contingent assets

Contingent liabilities and assets are not recognised in the Balance Sheet but are reported in the relevant schedules and notes. They may arise from uncertainty as to the existence of a liability or asset, or represent an existing liability or asset in respect of which settlement is not probable or the amount cannot be reliably measured. Contingent assets are reported when settlement is probable, and contingent liabilities are recognised when settlement is greater than remote.

There are no contingent liabilities or assets noted in these financial statements (2006: $0).

(u) Acquisition of assets

Assets are recorded at cost on acquisition except as stated below. The cost of acquisition includes the fair value of assets transferred in exchange and liabilities undertaken. Financial assets are initially measured at their fair value plus transaction costs where appropriate.

Assets acquired at no cost, or for nominal consideration, are initially recognised as assets and revenues at their fair value at the date of acquisition, unless acquired as a consequence of restructuring of administrative arrangements. In the latter case, assets are initially recognised as contributions by owners at the amounts at which they were recognised in the transferor authority's accounts immediately prior to the restructuring.

(v) Property, plant and equipment

Asset recognition and threshold

Purchases of property, plant and equipment are recognised initially at cost in the Balance Sheet, except for purchases costing less than $2,000, which are expensed in the year of acquisition (other than where they form part of a group of similar items which are significant in total).

The initial cost of an asset includes an estimate of the cost of dismantling and removing the item and restoring the site on which it is located. This is particularly relevant to 'makegood' provisions in property leases taken up by ARPC where there exists an obligation to restore the property to its original condition. These costs are included in the value of ARPC's leasehold improvements with a corresponding provision for the 'makegood' taken up.

Revaluations

Fair values for each class of asset are determined as shown below:

Asset class	Fair value measured at:
Leasehold improvements	Depreciated replacement cost
Plant & equipment	Market selling price

Following initial recognition at cost, property, plant and equipment are carried at fair value less accumulated depreciation and accumulated impairment losses. Independent valuations are conducted with sufficient frequency to ensure that the carrying amount of assets do not differ materially from the asset's fair value at the reporting date. The regularity of independent valuation depends upon the volatility of movements in market values for the relevant assets.

ARPC engaged an independent valuer, Herron Todd White, to conduct a valuation to determine the fair value of the property, plant and equipment as at 1 July 2004 and 30 June 2005.

Revaluation adjustments are made on a class basis. Any revaluation increment is credited to equity under the heading of asset revaluation reserve except to the extent that it reverses a previous revaluation decrement of the same asset class that was previously recognised through surplus and deficit. Revaluation decrements for a class of assets are recognised directly through surplus and deficit except to the extent that they reverse a previous revaluation increment for that class.

Any accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the asset restated to the revalued amount.

Depreciation

Depreciable property, plant and equipment assets are written-off to their estimated residual values over their estimated useful lives to ARPC using, in all cases, the straight-line method of depreciation. Leasehold improvements are depreciated on a straight-line basis over the lesser of the estimated useful life of the improvements or the unexpired period of the lease.

Depreciation rates (useful lives), residual values and methods are reviewed at each reporting date and necessary adjustments are recognised in the current, or current and future reporting periods, as appropriate.

Depreciation rates applying to each class of depreciable asset are based on the following useful lives:

	2007	**2006**
Leasehold improvements	**Lease term**	Lease term
Plant and equipment	**3 to 7 years**	3 to 7 years

The aggregate amount of depreciation allocated for each class of asset during the reporting period is disclosed in Note 11.

Impairment

All assets were assessed for impairment at 30 June 2007. Where indications of impairment exist, the asset's recoverable amount is estimated and an impairment adjustment made if the asset's recoverable amount is less than its carrying amount.

The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use. Value in use is the present value of the future cash flows expected to be derived from the asset. Where the future economic benefit of an asset is not primarily dependent on the asset's ability to generate future cash flows, and the asset would be replaced if ARPC were deprived of the asset, its value in use is taken to be its depreciated replacement cost.

All property, plant and equipment assets were assessed for indications of impairment as at 30 June 2007. There has been no impairment adjustment recognised in these financial statements (2006: $0).

(w) Intangibles

ARPC's intangibles comprise externally acquired and internally developed software for internal use. These assets are carried at cost.

Software is amortised on a straight-line basis over its anticipated useful life. The useful life of ARPC's externally purchased and internally developed software is 4 years (2006: 4 years).

All software assets were assessed for indications of impairment as at 30 June 2007. There has been no impairment adjustment recognised in these financial statements (2006: $0).

(x) Taxation

Income tax

ARPC is exempt from income tax by virtue of section 36 of the TI Act. ARPC is subject to fringe benefits tax and the goods and services tax (GST).

Revenues, expenses and assets are recognised net of the amount of GST:

- except where the amount of GST incurred is not recoverable from the Australian Taxation Office (ATO); and
- except for receivables and payables.

(y) Rounding of amounts

Amounts in these financial statements have been rounded to the nearest thousand dollars in accordance with policy 13.1(a) of the FMOs with the exception of:

- Executive remuneration;

- Members' remuneration;
- Auditor's remuneration; and
- transactions with related entities.

Note 2: Events after the Balance Sheet date

There have been no significant events occurring after the Balance Sheet date that would significantly affect these financial statements.

Note 3: Insurance contracts — risk management

The financial condition and operation of ARPC is affected by a number of key risks including insurance risk, liquidity risk, compliance risk, operational risk, interest rate risk and credit risk. Notes on ARPC's policies and procedures in respect of managing these risks are set out in this note.

Objectives in managing risks arising from insurance contracts and policies for mitigating those risks

Section 8 of the TI Act renders terrorism exclusion clauses in eligible insurance contracts ineffective. Insurers have the right to reinsure this risk with ARPC. ARPC's insurance risk is limited to eligible terrorism losses arising in respect of eligible insurance contracts.

ARPC's approach to managing risk is consistent with the Australian/New Zealand Standard for Risk Management (AS/NZS 4360:2004) and the Australian Prudential Regulation Authority's Prudential Standard GPS 220. The Board and senior management of ARPC have developed, implemented and maintain a sound and prudent Risk Management Strategy (RMS).

The RMS identifies ARPC's policies and procedures, processes and controls that comprise its risk management and control systems. These systems address all material risks, financial and non-financial, likely to be faced by ARPC. Annually, the Board reviews the RMS and confirms there are systems in place to ensure compliance with legislative and prudential requirements and that the Board has satisfied itself as to the compliance with the RMS. The RMS has been approved by the Board.

Key aspects of the process established to mitigate risks include:

- the capping of ARPC's liabilities at $10 billion plus the amount of the reserve for claims as a result of the effect of section 6(7) of the TI Act (specification of a reduction percentage if the Minister considers that, in the absence of a reduction percentage, the total amounts paid or payable by the Commonwealth would be more than $10 billion);

- the guarantee contained in section 35 of the TI Act by which the Commonwealth guarantees the payment of money that may become payable by ARPC to any person other than the Commonwealth. This guarantee would extend to any payments required to be made under the $1 billion commercial line of credit which ARPC has entered into;

- the development, maintenance and use of sophisticated management information systems, which provide up to date, reliable data on the risk to which the business is exposed at any point in time;

- the development of a standard reinsurance agreement for underwriting and accepting insurance risks;

- the collection of annual aggregate exposure data from clients to support advice given regarding a reduction percentage;

- the TI Act applies to all eligible insurance contracts. The wording of the TI Act was designed to ensure that ARPC's risk was diversified both geographically and by type of risk; and

- the mix of assets in which ARPC invests is regulated by section 18 of the *Commonwealth Authorities and Companies Act 1997*. The management of investments is closely monitored to ensure the liquidity of funds match the potential liabilities.

Interest rate risk

No financial assets or liabilities arising from insurance contracts entered into by ARPC are directly exposed to interest rate risk.

Credit risk

Financial assets and liabilities arising from insurance contracts are stated in the Balance Sheet at the amount that best represents the maximum credit risk exposure at balance date.

There are no significant concentrations of credit risk.

Terms and conditions of insurance

The terms and conditions attaching to insurance contracts affect the level of insurance risk accepted by ARPC. All insurance contracts are entered into in a standard form basis. There are no special terms and conditions in any contracts that have an impact on the financial statements.

Insurance contracts are reviewed annually.

Note 4: Revenue

		2007	2006
		$'000	$'000
(a)	**Premium revenue**		
	Gross written premium	**94,729**	103,204
	Movement in unearned premium reserve	**2,161**	(667)
	Total premium revenue	**96,890**	102,537
(b)	**Investment income**		
	Interest income	**18,803**	10,833
	Total investment income	**18,803**	10,833
(c)	**Other income**		
	Realised gain/(losses) recognised through the income statement	**5**	23
	Unrealised gain/(losses) recognised through the income statement	**-**	(8)
	Total other income	**5**	15
(d)	**Total revenue**	**115,698**	113,385

During the year ARPC was notified of two overpayments of gross written premium relating predominately to the June 2006 quarter end. After investigation, ARPC agreed to refund these overpayments. The impact of the refunds was to reduce gross written premium by $5,782,207 and increase the movement in unearned premium revenue by $5,059,431 million, thereby reducing total premium revenue by $722,776. The impact of the refunds are reflected in the 2006-07 financial results.

Note 5: Other operating expenses

The presentation of general and administration expenses in the income statement is by function. This note presents expenses according to their nature:

(a)	**Expenses by nature**			
	Employee expenses	5(c)	**1,585**	1,430
	Services from related entities		**177**	177
	Goods from external entities		**29**	31
	Services from external entities		**1,998**	1,776
	Operating lease rentals		**201**	217
	Depreciation and amortisation	11	**134**	65
	Bank fees and charges		**261**	268
	Total expenses by nature		**4,385**	3,964
(b)	**Expenses by function**			
	Acquisition costs		**412**	930
	General and administration expenses		**3,855**	3,034
	Investment expense		**118**	-
	Total expenses by function		**4,385**	3,964
(c)	**Employee expenses**			
	Wages and salaries		**1,298**	1,150
	Superannuation		**118**	112
	Leave and other entitlements		**155**	139
	Workers compensation premiums		**13**	12
	Other employee expenses		**1**	17
	Total employee expenses		**1,585**	1,430

Note 6: Cash and cash equivalents

	2007	2006
	$'000	$'000
Cash at bank	**91,508**	67,254
Total cash and cash equivalents	**91,508**	67,254

Cash and cash equivalents consist of at call deposits held with the Reserve Bank of Australia, Suncorp Metway Investment Management, Commonwealth Bank of Australia and St George Bank (2006: Reserve Bank of Australia and Suncorp Metway Investment Management).

Note 7: Receivables

Premium receivable	**22,496**	24,461
Interest receivable	**970**	750
GST receivable from the Australian Taxation Office	**26**	2
Total receivables	**23,492**	25,213

All receivables are with entities external to ARPC. Credit terms are net 30 days (2006: 30 days). Trade debtors are non-interest bearing.

Receivables (gross) are aged as follows:
Current

Less than 30 days	**23,492**	25,213
30 to 60 days	**-**	-
60 to 90 days	**-**	-
More than 90 days	**-**	-
	23,492	25,213

Interest receivable

The interest rate ranges from 5.65% to 6.38% (2006: 4.5% to 5.75%) and the frequency of payment is monthly.

Note 8: Investments under s18 of the CAC Act

Government securities	**-**	11,867
Term deposits	**263,000**	176,000
Total investments	**263,000**	187,867

Government Securities

Securities have terms of up to 3 years. They are guaranteed by the issuing Government and are traded in active markets. The effective interest rate is 0.00% (2006: 5.99%).

Term Deposits

Term deposits are held with the Reserve Bank of Australia, Suncorp Metway Investment Management Ltd and St George Bank and earn an effective rate of interest of 6.34% (2006: 5.89%). Interest is payable on maturity. Terms are between 17 and 96 days (2006:14 and 95 days).

Note 9: Deferred acquisition costs

	2007 $'000	2006 $'000
Deferred acquisition costs as at 1 July	**820**	466
Acquisition costs deferred	**392**	820
Amortisation charged to income	**(820)**	(466)
Deferred acquisition costs as at 30 June	**392**	820

Note 10: Other non-financial assets

Prepayments	**27**	**31**
Total other non-financial assets	**27**	**31**

All other non-financial assets are current assets.

Note 11: Property, plant and equipment and intangibles

(a)	**Buildings**		
	Leasehold improvements		
	- at cost	**306**	298
	- at valuation (fair value)	**47**	47
	- accumulated depreciation	**(107)**	(37)
	Total leasehold improvements	**246**	308
	Total buildings	**246**	308
(b)	**Plant and equipment**		
	- at cost	**75**	64
	- at valuation (fair value)	**110**	110
	- accumulated depreciation	**(93)**	(55)
	Total plant and equipment	**92**	119
(c)	**Total property plant and equipment**	**338**	427
(d)	**Intangibles - computer software**		
	- purchased	**41**	41
	- internally developed - in progress	**112**	-
	- internally developed - in use	**60**	60
	- accumulated amortisation	**(42)**	(16)
	Total computer software	**171**	85
	Total intangibles	**171**	85

All valuations are independent and are conducted in accordance with the revaluation policy stated at Note 1(v).

In 2004-05 the revaluations were performed by an independent valuer, Herron Todd and White (Canberra) Pty Limited.

No revaluation adjustment were made in the 2007 financial statements (2006: Nil).

Table A: Reconciliation of the opening and closing balances of property, plant and equipment and intangibles (2006-07)

Item	**Buildings leasehold improvements $'000**	**Plant & equipment $'000**	**Intangibles $'000**	**Total $'000**
As at 1 July 2006				
Gross book value	**345**	**174**	**101**	**620**
Accumulated depreciation/amortisation	**(37)**	**(55)**	**(16)**	**(108)**
Net book value 1 July 2006	**308**	**119**	**85**	**512**
Additions				
- by purchase	**8**	**11**	**-**	**19**
- internally developed - in progress	**-**	**-**	**112**	**112**
Depreciation/amortisation expense	**(70)**	**(38)**	**(26)**	**(134)**
Net book value 30 June 2007	**246**	**92**	**171**	**509**
Net book value as of 30 June 2007 represented by:				
Gross book value	**353**	**185**	**213**	**751**
Accumulated depreciation/amortisation	**(107)**	**(93)**	**(42)**	**(242)**
Net book value 30 June 2007	**246**	**92**	**171**	**509**

Table A: Reconciliation of the opening and closing balances of property, plant and equipment and intangibles (2005-06)

Item	Buildings leasehold improvements $'000	Plant & equipment $'000	Intangibles $'000	Total $'000
As at 1 July 2005				
Gross book value	76	117	81	274
Accumulated depreciation/amortisation	(14)	(27)	(2)	(43)
Net book value 1 July 2005	62	90	79	231
Additions				
- by purchase	269	57	8	334
- internally developed in use	-	-	12	12
Depreciation/amortisation expense	(23)	(28)	(14)	(65)
Net book value 30 June 2007	308	119	85	512
As at 30 June 2006				
Gross book value	345	174	101	620
Accumulated depreciation/amortisation	(37)	(55)	(16)	(108)
Net book value 30 June 2006	308	119	85	512

Note 12: Unearned premium liability

	2007	2006
	$'000	$'000
Unearned premium liabiilty as at 1 July	**48,350**	47,683
Deferral of premiums on contracts written in the period	**46,189**	48,350
Earning of premiums written in the previous periods	**(48,350)**	(47,683)
Unearned premium liability as at 30 June	**46,189**	48,350

During the year ARPC was notified of two overpayments of gross written premium relating predominately to the June 2006 quarter end. After investigation, ARPC agreed to refund these overpayments. The impact of these refunds are reflected in the 2006-07 financial results.

Unearned premiums are determined using the eighth system, a fractional method of calculation of the balance. This method is driven by the assumption that the risk attached to the revenue ceded expires evenly over each quarter of the financial year.

Note 13: Payables

Trade creditors	**120**	62
Unsettled investment transaction	**-**	12,021
Accruals	**314**	306
Total payables	**434**	12,389

Trade creditors:
Settlement is usually made net 30 days.

All of ARPC's liabilities are guaranteed by the Commonwealth by virtue of section 35 of the TI Act.

Note 14: Other interest bearing liabilities

Lease incentive	**6**	19
Other interest bearing liabilities are represented by:		
Current	**6**	13
Non-current	**-**	6
Total other interest bearing liabilities	**6**	19

Note 15: Provisions

		2007 $'000	2006 $'000
(a)	**Employee provisions**		
	Salaries and wages	**9**	17
	Leave	**231**	184
	Total employee provisions	**240**	201
	Current	**139**	133
	Non-current	**101**	68
	Total employee provisions	**240**	201
(b)	**Other provisions**		
	Make good provision	**49**	41
	Total other provisions	**49**	41

	Provision for make good $'000	Total $'000
Carrying amount at beginning of period	**41**	**-**
Additional provisions made	**-**	**41**
Present value adjustment	**8**	**-**
Amount owing at end of period	**49**	**41**

ARPC currently has an agreement for the leasing of premises which has a provision requiring ARPC to restore the premises to its original condition at the conclusion of the lease. ARPC has made provision to reflect the present value of this obligation.

All other provisions are non-current liabilities.

Note 16: Cash flow reconciliation

	2007 $'000	2006 $'000
Reconciliation of cash and cash equivalents as per Balance Sheet to Cash Flow Statement		
Report cash and cash equivalents as per:		
Cash Flow Statement	**91,508**	67,254
Balance Sheet	**91,508**	67,254
Difference	**-**	-
Reconciliation of operating result to net cash from operating activities		
Operating result	**111,313**	109,421
Depreciation/amortisation expense	**134**	65
Unrealised gains/(loss)	**-**	8
(Increase)/decrease in receivables	**1,721**	(1,037)
(Increase)/decrease in other non-financial assets	**4**	35
(Increase)/decrease in deferred acquisition costs	**428**	(354)
Increase/(decrease) in premium liability	**(2,161)**	667
Increase/(decrease) in payables	**66**	(28)
Increase/(decrease) in other interest bearing liabilities	**(13)**	19
Increase/(decrease) in provisions	**47**	147
Net cash from/(used by) operating activities	**111,539**	108,943

Note 17: Average staffing levels

	2007	2006
The average staffing levels for ARPC during the year were:	**13**	12

Note 18: Executive remuneration

	2007	2006
	$	$
The aggregate amount of total remuneration of executives shown below.	**1,056,751**	1,006,716

The number of senior executives who received or were due to receive total remuneration of $130,000 or more:		
$130,000 - $144,999	**1**	2
$160,000 - $174,999	**1**	1
$190,000 - $204,999	**1**	-
$205,000 - $219,999	**1**	1
$340,000 - $354,999	**1**	1
Total number of executives of ARPC	**5**	5

Note 19: Members' remuneration

	2007	2006
	$	$
Total remuneration received or due and receivable by Members of ARPC	**21,780**	40,128

The number of Members of ARPC included in these figures are shown below in the relevant remuneration bands:		
$ Nil - $14,999	**6**	5
$15,000 - $24,999	**-**	1
Total number of Members of ARPC	**6**	6

Note 20: Auditor's remuneration

	2007	2006
	$	$
The cost of financial statement audit services provided to ARPC was:	**110,000**	110,000

The financial statement audit services are provided to ARPC by the Auditor-General. No other services were provided by the Auditor-General during the reporting period.

Note 21: Related party disclosures

Members

The names of persons who were Members of ARPC during the financial year were:
Mr J Gersh, Mr A Lumsden, Ms M Micalizzi, Mr J Murphy, Ms M Rathbone and Mr G Vogt.

Changes in membership during the year:

Mr Gersh, Mr Lumsden, Ms Micalizzi were re-appointed for a further three year term from 1 July 2006.

Information on remuneration of Members is disclosed in Note 19.

Transactions with Members and Member related entities

ARPC has not entered into any contract with Members or their related entities.

Transactions with related entities

The service level agreement with the Department of the Treasury is considered a related party transaction. This agreement is for the provision of corporate support services to ARPC at a cost of $177,086 (2006: $176,512).

Controlling entity

ARPC was established by section 9 of the TI Act.

The ultimate controlling entity is the Australian Government. ARPC is only authorised to transact business and carry out functions as provided in the TI Act or as approved or directed by the Minister. ARPC's liabilities are guaranteed by the Commonwealth by virtue of section 35 of the TI Act.

Note 22: Contingent assets and contingent liabilities

Contingent assets

ARPC has no contingent assets

Contingent liabilities

ARPC has no contingent liabilities

Note 23: Segment reporting

ARPC was established under the TI Act to offer reinsurance for eligible properties within Australia against the risk of terrorism.

	2007	2006
	$'000	$'000
Gross written premium by geographical market:		
Australia	**83,498**	93,903
Overseas	**11,231**	9,301
Total gross written premium	**94,729**	103,204

All risks are located within the Australian market.

Note 24: Financial instruments

	Notes	Floating interest rate		Fixed interest rate maturing in				Non-interest bearing		Total		Weighted average effective interest rate	
				1 year or less		1 to 5 years							
		2007 $'000	2006 $'000	**2007 $'000**	2006 $'000	**2007 $'000**	2006 $'000	**2007 $'000**	2006 $'000	**2007 $'000**	2006 $'000	**2007 $'000**	2006 $'000
(a) **Interest rate risk**													
Financial assets													
Cash and cash equivalents	6	**91,508**	67,254	**-**	-	**-**	-	**-**	-	**91,508**	67,254	**6.21%**	5.70%
Receivables (gross)	7	**-**	-	**-**	-	**-**	-	**23,492**	25,213	**23,492**	25,213	**n/a**	n/a
Government securities	8	**-**	-	**-**	-	**-**	11,867	**-**	-	**-**	11,867	**0.00%**	5.99%
Fixed term deposits	8	**-**	-	**263,000**	176,000	**-**	-	**-**	-	**263,000**	176,000	**6.34%**	5.89%
Total		**91,508**	67,254	**263,000**	176,000	**-**	11,867	**23,492**	25,213	**378,000**	280,334		
Total assets										**378,928**	281,697		
Financial liabilities													
Payables	13	**-**	-	**-**	-	**-**	-	**434**	12,389	**434**	12,389	**n/a**	n/a
Total		**-**	-	**-**	-	**-**	-	**434**	12,389	**434**	12,389		
Total liabilities										**46,918**	61,000		

Note 24: Financial instruments (continued)

	Notes	Total carrying amount 2007 $'000	Aggregate net fair value 2007 $'000	Total carrying amount 2006 $'000	Aggregate net fair value 2006 $'000
(b) **Fair value of financial assets and liabilities**					
Financial assets					
Cash at bank	6	**91,508**	**91,508**	67,254	67,254
Receivables (net)	7	**23,492**	**23,492**	25,213	25,213
Government securities	8	**-**	**-**	11,867	11,867
Fixed term deposits	8	**263,000**	**263,000**	176,000	176,000
Total finanical assets		**378,000**	**378,000**	280,334	280,334
Financial liabilities					
Payables	13	**434**	**434**	12,389	12,389
Total financial liabilities		**434**	**434**	12,389	12,389

Financial assets

The net fair values of cash at bank, fixed term deposits and non-interest bearing monetary financial assets are recognised at their carrying amounts.

The net fair values of Government securities is market value.

Financial liabilities

The net fair value for payables, all of which are short term in nature, are recognised at their carrying amounts.

(c) **Credit risk exposures**

ARPC's maximum exposures to credit risk at reporting date in relation to each class of recognised financial assets is the carrying amount of those assets as indicated in the Balance Sheet.

ARPC has no significant exposures to any concentration of credit risk.

(d) **Other disclosures**	**2007 $'000**	2006 $'000

In the event of a declared terrorist incident ARPC has unrestricted access to the following line of credit:

Bank standby facility	**1,000,000**	1,000,000
Amount of facility used as at 30 June	**-**	-
Facility available:	**1,000,000**	1,000,000

Any payment which becomes due under the facility agreement is guaranteed by the Commonwealth by virtue of section 35 of the TI Act.

In the event of a declared terrorist incident ARPC has access to the following Commonwealth indemnity:

Commonwealth indemnity	**9,000,000**	9,000,000
Amount of facility used as at 30 June	**-**	-
Facility available:	**9,000,000**	9,000,000