

BUDGET ESTIMATE 2022-23



Economics Legislation Committee



Australian Government

Australian Reinsurance Pool Corporation

Budget Estimates 2022-23

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Hearing Program including committee outline

Refer to website

https://www.aph.gov.au/Parliamentary_Business/Senate_estimates/Economics/2022-23_Budget_estimates_November

Senator Jess Walsh (*Chair*) – Australian Labor Party, Victoria



Senator Deborah O'Neill – Australian Labor Party, New South Wales



Senator Jana Stewart – Australian Labor Party, Victoria



Senator Andrew Bragg (*Deputy Chair*) – Liberal Party of Australia, New South Wales



Senator Nick McKim – Australian Greens (Whip), Tasmania



Senator Dean Smith – Liberal Party of Australia, Western Australia



Budget Estimates - 9 November 2022

Opening Statement by Dr Chris Wallace, Chief Executive, Australian Reinsurance Pool Corporation

Thank you Chair, and members of the Committee for the invitation to appear today.

I would like to start by acknowledging the Ngunnawal people, Traditional Custodians of the land on which we meet today and pay my respects to their Elders past and present.

The Australian Reinsurance Pool Corporation's purpose is to protect Australian Communities with sustainable and effective reinsurance for terrorism and cyclone events.

ARPC is a public financial corporation within the Treasury Portfolio. The Corporation is established by legislation and governed by our Accountable Authority, which is the ARPC Board.

ARPC operates in a commercial context as a service provider in the reinsurance sector, with insurance organisations being ARPC's customers. The Corporation is funded through reinsurance premiums charged to insurers.

ARPC's reinsurance premium is expected to reach \$1.1 billion for both terrorism and cyclone reinsurance pools when fully established.

ARPC was established under the Terrorism Insurance Act on the 1 July 2003 to administer the Terrorism Reinsurance Pool. This was in response to the global withdrawal of terrorism insurance cover by insurers, following the 11 September 2001 attacks in the US. The legislation requires that ARPC provide reinsurance cover for eligible terrorism losses to Australia's commercial property insurers.

There is still no whole of market, sustainable alternative terrorism reinsurance cover available, and the current Australian terrorism threat level remains at *probable*. ARPC currently provides insurers with an annual funding capacity of \$14.2bn in the event of a loss. This includes ARPC net assets, retrocession reinsurance that ARPC purchases and \$10 billion commonwealth guarantee.

Last year's review of the legislation by Treasury recommended that ARPC continue to provide terrorism re-insurance cover.

ARPC welcomed the passing of legislation in late March this year, which established the cyclone reinsurance pool to be administered by ARPC.

The cyclone pool will cover losses caused by cyclonic winds, cyclone related flooding and storm surge. We estimate it will cover 3.3 million households, 220,000 small businesses, and 140,000 residential strata and small commercial strata properties.

The cyclone pool operates Australia wide, but targets premium reductions on home, commercial and strata insurance for eligible consumers in cyclone-prone areas. These are mainly in northern Australia. It is underpinned by a \$10 billion Commonwealth guarantee, which can be adjusted in the legislation.

ARPC's corporate plan outlines our strategic priorities, which include delivering reinsurance for eligible terrorism and cyclone losses. ARPC commenced substantive preparations for the cyclone pool in November 2021. We established a dedicated project team, focused on implementing the new pool and commenced the processes for systems development, and actuarial determination of premiums.

ARPC is working closely with insurer customers to enable their onboarding to the cyclone pool. We are focused on making our support to insurers as efficient and effective as we can.

We have consulted with insurers and provided them with a reinsurance agreement, insurer onboarding procedures, catastrophe modelling, and data requirements.

We have released modelling and provided premium rates, that will support our effort to deliver the best and most affordable outcomes to insurers and consumers. While it is mandatory for large insurers to transfer all risks to the pool by 31 December 2023, and for small insurers by 31 December 2024, ARPC is ready to receive risk now.

The key matters of interest to various stakeholders have been on what the cyclone pool will look like, how it will work, and what effect it will have on insurance premiums in cyclone prone regions across Australia.

ARPC looks forward to further working with the insurance industry and educating the community to make a success of the new cyclone pool across cyclone-prone regions.

The Corporation is currently going through significant growth, increasing in size and complexity. We are building on our sound foundations to administer both the Terrorism pool and Cyclone pool. This is a very significant change for the insurance industry as well.

I am confident we will deliver our legislative obligations as well as continue to contribute to insurance affordability and in the longer term insurance risk mitigation for Australian communities.

With that, I am pleased to take Committee Member's questions.

1. ARPC (source Corporate Plan 2022-2026)

1.1 About ARPC

- Australian Reinsurance Pool Corporation (ARPC)
- ARPC is a Corporate Commonwealth entity, Financial Corporation and Treasury portfolio agency.
- Established by the *Terrorism Insurance Act 2003* (TI Act) in 2003.
- ARPC was established in 2003 by the Australian Government to provide reinsurance cover for eligible terrorism losses.
- This followed the September 11, 2001, terrorist attacks in the United States after which terrorism cover was excluded from commercial and industrial property policies around the world and in Australia.
- On 31 March 2022, the legislation was amended to become the *Terrorism and Cyclone Insurance Act 2003* (TCI Act), conferring responsibility on ARPC for the administration of a cyclone reinsurance pool.

1.2 PURPOSE

- Protecting Australian communities with sustainable and effective reinsurance for terrorism and cyclone events.

1.3 VISION

- To support insurers to deliver affordable terrorism and cyclone insurance in Australia.

1.4 CORPORATE VALUES

- Collaboration, Delivering for our stakeholders, Personal Leadership, Integrity, Wellbeing.

1.5 STRATEGIC PRIORITIES

There are six strategic priorities in the 2022-26 Corporate Plan. Activities are focused around delivering against these priorities.

- Deliver reinsurance for eligible terrorism and cyclone losses.
- Engage and understand our stakeholders, with a focus on insurer customers to improve community outcomes.
- Develop data and insights on terrorism, cyclone, and insurance climate risk to support risk mitigation
- Enhance thought leadership to fulfill our role as a trusted advisor
- Be a high performing, inclusive, customer-centred and risk focused culture
- Establish the cyclone pool, enhance operational effectiveness, and event preparedness.

2. LEGISLATION (*source Federal Register of Legislation*)

2.1 TCI ACT FUNCTIONS

ARPC's functions under section 10 of the TCI Act are:

- to provide insurance cover for eligible terrorism losses (whether by entering contracts or by other means)
- to operate a cyclone and related flood damage reinsurance pool by entering contracts of reinsurance as reinsurer in accordance with Part 2A and
- any other functions that are prescribed by the regulations.

Key Dates

- Terrorism Insurance Act 2003 – Date of Assent 24 June 2003
- Terrorism and Cyclone Insurance Act 2003 – Date of Assent 31 March 2022 in response to Treasury Laws Amendment (Cyclone and Flood Damage Reinsurance Pool) Act 2022.

2.2 TCI REGULATIONS

TCI Regulations supports the operation of the TCI Act by providing:

- Terrorism insurance definitions, contents, residential, eligible property, and schedule of exclusions for a contract of insurance.
- Cyclone insurance definitions for cyclone, end or reintensifies, eligible property, strata or community title development, eligible insurance contract exclusions, premium income threshold, pool insurance contract, storm surge & flood, end of claims period, and content of Financial Outlook Report.

Key Dates

- Terrorism Insurance Regulations 2003 – Date of commencement 1 July 2003
- Terrorism Insurance Regulations 2003 – Date of commencement 16 October 2021 in response to Terrorism Insurance Amendment (Cyclones and Related Flood Damage) Regulations 2021 – new function of ARPC to prepare for the operation of a cyclones and related flood damage reinsurance pool.
- Terrorism and Cyclone Insurance Regulations 2003 Date of commencement 5 April 2022 – introduction of Cyclone and Flood Related Damage Reinsurance Pool.

3. CHIEF EXECUTIVE (CE) (source Federal Register of Legislation)

3.1 DUTIES

- Section 24 of TCI Act sets out the duties of CE:
- to manage the affairs of the Corporation subject to the directions of, and in accordance with policies determined by, the Corporation
- a thing is taken to have been done by the Corporation if it is done in the name of the Corporation, or on behalf of the Corporation:
 - by the CE; or
 - with the authority of the CE.

4. ARPC BOARD & COMMITTEE *(source Annual Report 2021/22)*

4.1 BOARD

- ARPC's (the Corporation) Accountable Authority (the Board) is constituted under section 12 of the TCI Act.
- The Board composition:
 - a Chair;
 - at least 6, but not more than 8, other members.
 - There are currently 2 vacant positions.
- Members are appointed in writing by the Minister, on a part-time basis, for a specific term set out in the instrument of appointment. Term period must not exceed 4 years.
- Members are remunerated in accordance with the Remuneration Tribunal *(Remuneration and Allowances for Holders of Part-time Public Office) Determination 2022 – Part 6*. The current remuneration is:

	Base Fee	Meeting Fee	Travel Tier
Chair	\$28,510	\$1,199	1
Member	\$14,260	\$1,079	1

- Current Members:
 - Mr Ian Carson AM (Chair) – 1 July 2017 to 30 June 2023
 - Ms Elaine Collins – 1 Jul 2015 to 30 Jun 2021 & 1 Jul 2021 to 30 Jun 2024
 - Ms Robin Low – 5 Oct 2016 to 4 Oct 2019 & 23 Apr 2020 to 22 Apr 2023
 - Ms Maria Fernandez – 23 Apr 2020 to 22 Apr 2023
 - Mr David Foster – 16 Dec 2021 to 15 Dec 2024
 - Ms Julie-Anne Schafer – 14 Sep 2021 to 13 Sep 2024
 - Mr Jan van der Schalk – 1 Jul 2021 to 20 Jun 2024

4.2 COMMITTEE

- In accordance with section 45 of the PGPA Act, the Board has established an Audit, Risk and Compliance Committee. The Committee supports the Board overseeing the administration and governance of ARPC.
- The Committee must consist of at least 3 appropriately qualified and skilled Members (section 17 of PGPA Rule).
- The functions of the Committee are set out in its Charter and include reviewing the appropriateness of ARPC's:
 - financial report
 - performance reporting
 - system of risk oversight and management and
 - system of internal controls.
- The Committee Chair reports verbally to each Board meeting and in writing annually.

4.2 OBSERVERS *(source Federal Register of Legislation)*

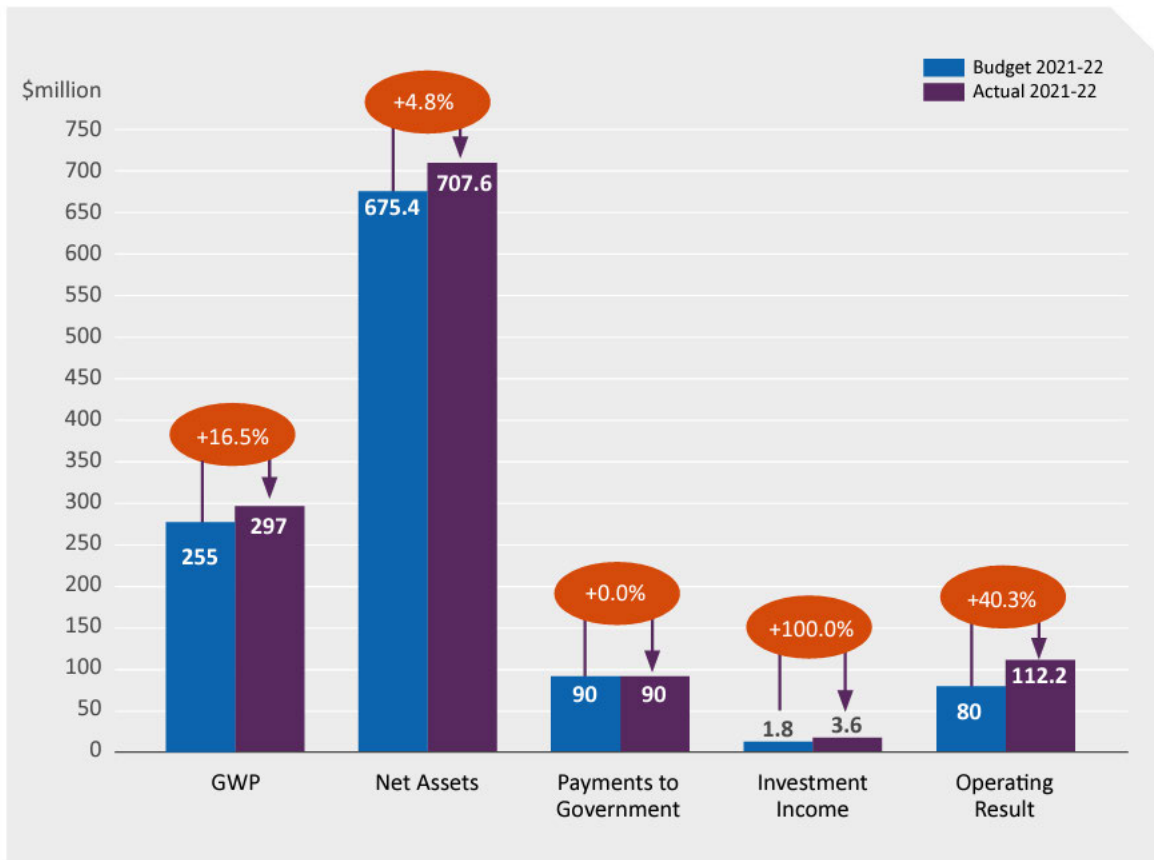
- The TCI Act section 20A enables the Minister to appoint 2 observers to the Board.
- An Observer holds office for the period specified in the instrument of appointment. The period must not exceed 2 years.

4.3 ROLE of observers:

- is entitled to receive notice of meetings of ARPC
- may attend any meeting of ARPC and take part in the proceedings (excluding voting), as the observer thinks fit
- may report to the Minister on any matter relating to the cyclone reinsurance scheme; and
- if the Minister requests a report on such a matter, must report to the Minister on that matter.
- Current appointed observers are:
 - Ms Helen Rowell, APRA
 - Mr Guy Thorburn, AGA

5. ARPC FINANCES (source Annual Report 2021/22)

5.1 Summary of key financial metrics FY2021-22



Financial snapshot

Figure 4.1: ARPC by numbers as at 30 June 2022



5.2 Expenditure including Year to Date FY2022-23, with Budget comparison

Expenditure	Year to Date Sept 2022	FY 22/23 Budget	FY2021/22	FY2020/21
Total Expenditure	4,982,968	27,700,000	16,800,000	9,766,000
Expense Cyclone Implementation	2,870,525	17,500,000	8,361,807	345,010
Cost of Core Reinsurance System	577,403	1,670,000	811,469	30,385
Consultants	1,507,939	10,704,000	6,991,310	2,814,945
Legal Services	68,965	250,000	371,586	121,570
Leases	203,113	814,000	520,058	386,773
Gifts and Benefits	0	0	374	1,123
Bonus Payments	0	0	0	0
International Travel	0	300,000	0	0
Cost of Actuarial Spend – Finity Cyclone	460,537	2,400,000	1,772,806	32,377
Cost of Actuarial Spend – Finity Non-Cyclone	22,522	20,000	197,666	237,718

- Consultants' costs are made up of several projects which have not yet started and therefore the run rate is below budget for now.
- The recent travel for the retro renewals will be expensed in October. The \$300k budget will be the actual cost this financial year based on actual quotes received and trips booked to date.

5.3 Key Management Personnel Salary Note

- Annual report – key management personnel salary for the period 1 July 2021 to 30 June 2022.
- The accrued and paid annual leave has been added and included to the LSL column.
- This should instead have been included in the base salary amount as it is a short-term benefit.
- The difference is approximately \$40k to the base salary and LSL totals (contra) which equates to 1.8% of the total remuneration value.

- The total remuneration per employee is correct as is the total remuneration figure.
- The annual audited financial statements are not impacted by this.
- This is a standalone table.

Name	Position	Short Term Benefits			Long Term Benefits		Termination Benefits	Total Remuneration
		Base Salary	Bonuses	Other Allowances	Superannuation Contributions	LSL		
Carson, Ian	Chair	\$28,906	–	\$4,664	\$2,891	–	–	\$36,460
Collins, Elaine	Member	\$14,920	–	\$4,200	\$1,492	–	–	\$20,612
Low, Robin	Member	\$14,920	–	\$3,150	\$1,492	–	–	\$19,562
Fernandez, Maria	Member	\$14,920	–	\$4,200	\$1,492	–	–	\$20,612
Schafer, Julie-Anne*	Member	\$10,776	–	\$4,550	\$1,078	–	–	\$16,404
van der Schalk, Jan**	Member	\$13,337	–	\$4,200	\$1,334	–	–	\$18,870
Foster, David***	Member	\$7,202	–	\$3,150	\$720	–	–	\$11,072
Wallace, Christopher	CEO	\$398,149	–	–	\$39,354	\$29,919	–	\$467,422
Pennell, Michael	CUO	\$295,086	–	–	\$29,515	\$6,659	–	\$331,261
Park, John	CFO	\$276,277	–	–	\$27,634	\$20,685	–	\$324,596
Williams, Helen	COO	\$276,413	–	–	\$27,648	\$6,613	–	\$310,673
Lawrence, Samantha	CRGO	\$272,394	–	–	\$27,239	\$1,204	–	\$300,838
Flanagan, Jason****	CCCO	\$166,181	–	–	\$16,618	\$15,294	–	\$198,093
Matruglio, Peter*****	ICFO	\$83,732	–	–	\$8,373	–	–	\$92,105
		\$1,873,212	–	\$28,114	\$186,881	\$80,374	–	\$2,168,580

* Commenced 14 Sep 2021

** Commenced 01 Jul 2021

*** Commenced 16 Dec 2021

**** Commenced 22 Nov 2021

***** Commenced 26 April 2022

Below is the correct figures for key management personnel.

Key Management Personnel									
Name	Position title	Short-term benefits			Post-employment benefits	Other long-term benefits		Termination benefits	Total remuneration
		Base salary	Bonuses	Other benefits & allowances	Superannuation contributions	Long service leave	Other long-term benefits		
Carson, Ian	Chair	\$ 28,906	\$ -	\$ 4,664	\$ 2,891	\$ -	\$ -	\$ -	\$ 36,460
Collins, Elaine	Member	\$ 14,920	\$ -	\$ 4,200	\$ 1,492	\$ -	\$ -	\$ -	\$ 20,612
Low, Robin	Member	\$ 14,920	\$ -	\$ 3,150	\$ 1,492	\$ -	\$ -	\$ -	\$ 19,562
Fernandez, Maria	Member	\$ 14,920	\$ -	\$ 4,200	\$ 1,492	\$ -	\$ -	\$ -	\$ 20,612
Shafer, Julie-Anne	Member	\$ 10,776	\$ -	\$ 4,550	\$ 1,078				\$ 16,404
Van Der Schalk, Jan	Member	\$ 13,337	\$ -	\$ 4,200	\$ 1,334				\$ 18,870
Foster, David	Member	\$ 7,202	\$ -	\$ 3,150	\$ 720				\$ 11,072
Wallace, Christopher	Chief Executive	\$ 415,769	\$ -	\$ -	\$ 39,354	\$ 12,299	\$ -	\$ -	\$ 467,422
Pennell, Michael	Chief Underwriting Officer	\$ 296,875	\$ -	\$ -	\$ 29,515	\$ 4,870	\$ -	\$ -	\$ 331,261
Park, John	Chief Financial Officer	\$ 286,852	\$ -	\$ -	\$ 27,634	\$ 10,110	\$ -	\$ -	\$ 324,596
Williams, Helen	Chief Operating Officer	\$ 277,386	\$ -	\$ -	\$ 27,648	\$ 5,640	\$ -	\$ -	\$ 310,673
Lawrence, Samantha	Chief Governance Officer	\$ 268,332	\$ -	\$ -	\$ 27,239	\$ 5,266	\$ -	\$ -	\$ 300,838
Flanagan, Jason	Chief Claims and Customer Officer	\$ 178,904	\$ -		\$ 16,618	\$ 2,571			\$ 198,093
Matruglio, Peter	Interim Chief Financial Officer	\$ 83,732	\$ -		\$ 8,373	\$ -			\$ 92,105
Total		\$ 1,912,830	\$ -	\$ 28,114	\$ 186,881	\$ 40,756	\$ -	\$ -	\$ 2,168,580

- Murray motion reporting for period 1 July 2021 to 30 June 2022 as shown on ARPC website
- The Murray Motion lists the contracted salary figures.
- The Annual report table shows the expense for the year.
- They will differ due to the amount of leave taken, staff leaving and starting part way through the year.

Contractor	Subject Matter	Amount of Consideration	Start date	Anticipated end date
CUO of ARPC	Non-APS staff contract engaged directly	\$325,712 p.a.	25/8/2003	ongoing
CEO of ARPC	Non-APS staff contract engaged directly	\$441,658 p.a.	9/12/2013	ongoing
CFO of ARPC	Non-APS staff contract engaged directly	\$286,000 p.a.	26/4/2022	ongoing
COO of ARPC	Non-APS staff contract engaged directly	\$305,100 p.a.	20/10/2019	ongoing
CRGO of ARPC	Non-APS staff contract engaged directly	\$308,426 p.a.	1/03/2021	ongoing
CCCO of ARPC	Non-APS staff contract engaged directly	\$320,000 p.a.	22/11/2021	Ongoing

6. ARPC PEOPLE *(source Annual Report 2021/22)*

6.1 SENIOR EXECUTIVE TEAM

- ARPC's Senior Executive team is headed by the Chief Executive, who was appointed by the Corporation under the TCI Act.
- The current Leadership team comprises:
 - Dr Christopher Wallace – Chief Executive
 - Mr Jason Flanagan – Chief Claims and Customer Officer
 - Ms Samantha Lawrence – Chief Risk and Governance Officer
 - Mr Michael Pennell, PSM – Chief Underwriting Officer
 - Mr Peter Matruglio – Interim Chief Financial Officer
 - Ms Rachael Glasson – Acting Chief Operating Officer (in tandem with Mr Grant Ironside).

6.2 ONGOING/NON-ONGOING EMPLOYEES

- As at 30 June 2022, ARPC had 35 employees, an increase of 40% from 25 employees in the previous reporting period.
- The growth in staffing numbers is attributable to the increased resourcing required to prepare for, and administer, the cyclone pool.
- All employees are Sydney based – 33 full time, 2 are part time.

6.3 CONTRACTORS

- As at 30 June 2022, ARPC engaged 8 contractors to assist with the planning for/ and implementation of the cyclone pool.
- Contractors were engaged as technical consultants to fulfil short-term knowledge acquisition and resourcing needs (actuarial (1), underwriting (1), project management (4), risk management (1), and recruitment (1)).

6.4 DIVERSITY STATS

- The average age of employees is 43 years, and 54% are women.
- ARPC's recruitment processes and ongoing operational activities strives to provide a diverse workplace providing equal opportunity employment (EEO). Our 'office-first' hybrid working environment allows employees to work either on site or remotely, and within extended hours.
- As at 30 June 2022, ARPC had met the Australian Government's indigenous employment target of 3% which was set in response to the Forrest Review, this was achieved by recruiting an indigenous intern. This is the 4th consecutive year ARPC has proudly supported the Career Trackers.

Figure 6.1: Number of permanent employees by organisational level (classification) and gender, as at 30 June 2022.

	Male			Female			Combined total
	Full time	Part time	Total	Full time	Part time	Total	
ARPC level 2	1	–	1	–	–	–	1
ARPC level 3	–	–	–	–	–	–	–
ARPC level 4	1	–	1	–	1	1	2
ARPC level 5	–	–	–	1	–	1	1
ARPC level 6	1	–	1	4	–	4	5
EL 1	2	–	2	6	–	6	8
EL 2	7	–	7	4	1	5	12
SES*	4	–	4	2	–	2	6
Total	16	–	16	17	2	19	35

*SES = Senior Executive Service staff

6.5 RECRUITMENT

- Currently there were 25 vacant positions, which is the balance of approved positions to administer both the terrorism and cyclone pools.
- Recruitment is a priority and is ongoing.

6.6 KEY PEOPLE ISSUES

- High volume of recruitment activity in a competitive market, in a short period of time.
- Delayed approval of enterprise agreement through APSC and Fair Work.

6.7 ENTERPRISE AGREEMENT

- The current ARPC EA expired in May 2022, although continues to be in effect until replaced by a new instrument.
- The proposed EA is awaiting approval from Australian Public Service Commission (APSC) under the recently released Interim Employee Relations Policy.
- Remuneration increases have been delayed by 6 months.
- ARPC has not paid performance bonuses to staff for last 3 years.
- ARPC has strictly complied with government guidelines in respect of employee relations matters.
- ARPC has strong relationships with both the APSC and Treasury and Treasury Sub Departments.

Enterprise Agreement

- The draft Enterprise Agreement has received in-principle approval from the APSC Commissioner.
- It is now being put forward for the Commission's final review and approval.

Senior Employee Remuneration

- ARPC has communicated an intent to uplift remuneration for employees in specific senior roles to the ASPC.
- The Minister's Office and Treasury have also been briefed.
- The market remuneration changes for senior employees (SES and EL2) apply to 13 out of 20 senior staff based on an independent report produced by Mercer.
- The change sees all SES roles (6) receiving an increase (varying amounts), and 50% of EL2 roles will receive an increase (varying amounts).
- The increase amounts for all individuals vary depending on the role, from 1% to 20% (the average increase, 10%).
- We are currently in discussion with the APSC on this matter.

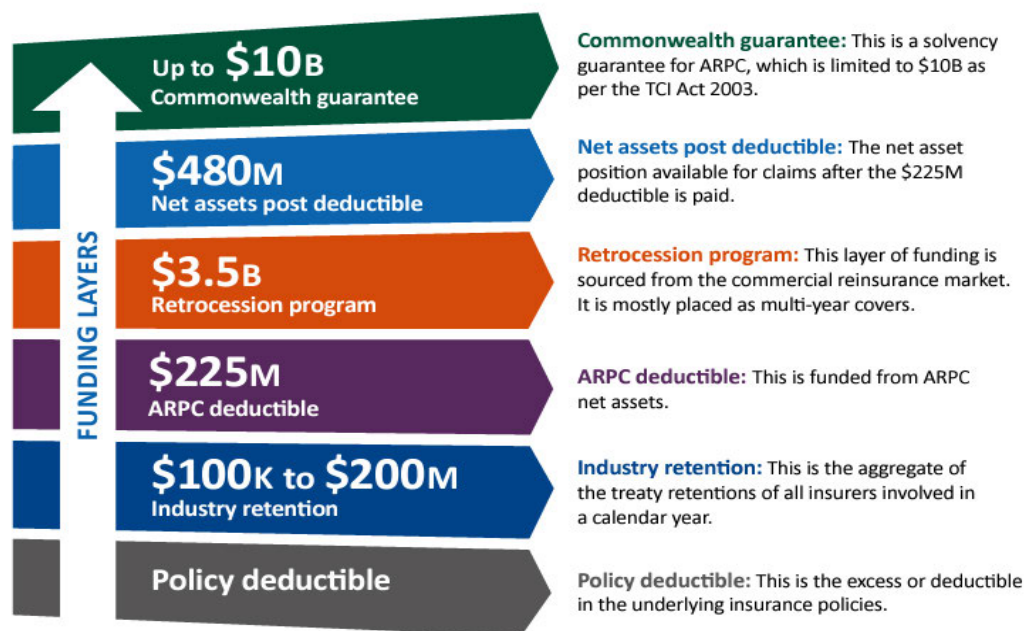
7. TERRORISM REINSURANCE POOL *(source Annual Report 2021/22)*

- Australia's terrorism reinsurance scheme was established after discussion with key industry stakeholders, including insurance and reinsurance companies, banks, representatives of property owners, industry associations, insurance brokers and actuaries.
- Through the scheme, insurance companies can choose to reinsure the risk of claims for eligible terrorism losses by entering into a treaty Agreement with ARPC and paying premiums to ARPC. Eligible contracts of insurance are defined in Terrorism Insurance Act. The policy holders of eligible insurance contracts will be covered for eligible terrorism losses in the event of a declared terrorist incident (DTI), with insurers required to meet these claims in accordance with the other terms and conditions of individual policies.
- Claims against the scheme are met once an individual insurance company's retention is exhausted. ARPC's pool of retained earnings will meet claims until the agreed retrocession deductible is reached. At this point claims are funded by the retrocession program. Once retrocession is exhausted, claims will continue to be met by the Commonwealth guarantee.
- The total value of the scheme is approximately \$14 billion.

7.1 REDUCTION PERCENTAGE

- If the responsible Minister considers that the amount paid or payable under the Commonwealth guarantee will exceed \$10 billion, the Minister must also announce a reduction percentage. This will have the effect of limiting the level of cover, by reducing the amount payable by the insurer to the policy holder.

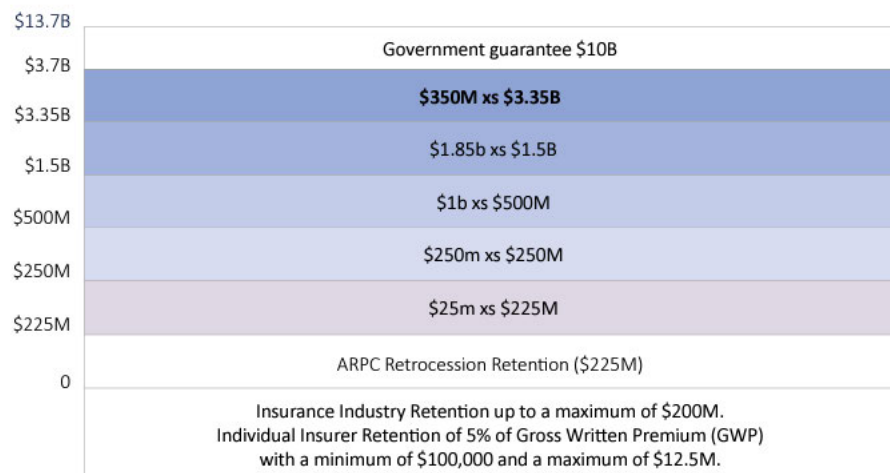
2021 TERRORISM REINSURANCE POOL STRUCTURE



7.2 RETROCESSION PLACEMENT

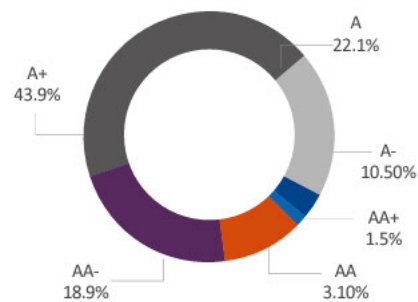
- ARPC's retrocession program continues to provide the following benefits:
 - Increases overall terrorism pool capacity
 - Positions the Commonwealth further from the risk of terrorism losses under the pool
 - Reduces the likelihood that a reduction percentage will be required
 - Facilitates inflow of foreign funds to rebuild Australian assets following a terrorism incident, and
 - Encourages the return of the commercial terrorism insurance and reinsurance market for Australian risks.
- The retro program renews on 1 January of each year. The 2022 placement of \$3.5 billion includes \$2.57 billion in capacity previously written on a multi-year basis was instead place on a rolling three-year agreement, with a cancel and replace structure, to reduce pricing volatility for ARPC and its retrocessionaires. A best in market deficit clause was also drafter and agreed to for the 2022 placement.

Figure 2.4: Retrocession program detail



- The retro program has 67 participants from the Australian market and from the Lloyds, European, Bermudian, USA, and Asian Markets.

Figure 2.5 Retrocession program counterparty credit rating for the 2022 calendar year



7.3 TRIENNIAL REVIEWS

- Section 41 of the TCI Act requires that at least once every 3 years the Minister is to prepare a report that test whether terrorism insurance market failure exists, and therefore, whether both the Act and ARPC should continue.
- Previous review has also been used as an opportunity to improve and refine the terrorism pool.
- Finding from the 2021 Triennial Review published in Dec 2021 found:
 - that in ARPC's absence, a market failure in terrorism insurance markets covering physical property would likely re-emerge and recommended that the Act remain
 - cyber terrorism is an evolving market and yet to show market failure in relation to physical property damage
 - interactions between the cyclone and terrorism pools and Board arrangements:
 - expand Board size
 - appoint Members with experience in the insurance pressures of residents in cyclone prone areas
 - appoint 2 Board observers – from APRA and AGA
- The amendment to the Act for cyclone changed section 41 from 3-year reviews to 5-year reviews (after 1 July 2025).

7.4 CYBER CRIME EXCLUSION (source Treasury Triennial Reviews

<https://arpc.gov.au/reinsurance-pools/the-act/#triennial-reviews>)

- The Triennial Review 2018 identified emerging issues around Cyber terrorism causing damage to property and incidents causing harm to people.
- The Treasury review identified:
 - Cyber terrorism is an emerging risk and there is yet to be a clear and evident market failure in relation to physical property damage from cyber terrorism requiring government intervention through the Act at this time.
 - Coverage is broad for domestic terrorism incidents causing death or serious injury to Australians. There is an array of government schemes under which they could claim some form of compensation or funding, depending on their circumstances. There are also widely available insurance products that do not contain exclusions for terrorism incidents.
- The Triennial Review 2021 confirmed the findings from the 2018 review. Specifically, cyber insurance is an evolving market and there is yet to be a clear and evident market failure in relation to physical property damage from cyber terrorism.
- The review also recommended that the Act maintains its current 'computer crime' exclusion.

8. TERRORISM PREMIUM RATES (source Annual Report 2021/22)

- ARPC's premium and investment income is used to:
 - Fund its operations and build a reserve to meet future claims
 - Pay retrocession premiums
 - Pay any fees and dividends to the Australian Government for the provision of the Commonwealth guarantee.
- The premium charged by ARPC for reinsurance is determined by Ministerial Direction.

Figure 2.2: Tier rates

Premium Tier	Current rate
A	16% of gross base premium
B	5.3% of gross base premium
C	2.6% of gross base premium

- Premium tiers are set by a postcode's population density

Premium Tier	Geographical location
A	Major CBD areas of Australian cities (Sydney, Melbourne, Brisbane, Perth and Adelaide)
B	Urban areas of all Australian state and territory cities with a population usually exceeding 100,000 (Sydney, Melbourne, Brisbane, Perth, Adelaide, Gold Coast, Canberra, Newcastle, Central Coast of New South Wales, Wollongong, Hobart, Geelong, Sunshine Coast of Queensland, Townsville, Darwin, Cairns and Toowoomba)
C	Australian postcodes not allocated to either tier A or B and representing a physical address, as well as any property not on the mainland of Australia or Tasmania, but within the coastal sea of Australia

9. CYCLONE REINSURANCE POOL (source Annual Report 2021/22)

- The cyclone pool covers the cost of cyclone and cyclone-related flood damage for:
 - 3.3 million homes for building and contents
 - 220k small businesses for building, contents and business interruption
 - 140k residential and small commercial strata buildings
- The pool is covered by a \$10b government guarantee that will be increased in the case where a large cyclone event, or series of events, is likely to exceed this amount.
- Aims of the scheme:
 - To be cost-neutral in the long term
 - Not to make a profit
 - To lower insurance costs for medium and high-risk properties
 - To maintain risk reduction incentives and offer discounts for risk mitigation
 - To encourage mitigation
- The CRP will not charge a margin for the risk it takes on. Low risk properties will be charged the same amount as they were prior to the pool, and the margins that were previously paid will be used to cross-subsidise medium and high-risk properties.
- Premiums will be more stable as they will not need to respond to market cycles and pressures.
- Premiums have been set at the individual risk level, using data such as geography, building characteristics and mitigations.
- ARPC have spent \$8.3m compared to forecast \$22.6m on setting up the operations of the cyclone pool. The remainder has been carried over the next financial year. 17 new staff were appointed.
- Delivered so far:
 - Reinsurance agreement
 - Initial premium rates
 - Additions to website
 - Electronic file sharing
 - New platform to onboard customers, collect premiums and manage events

- Coordination with BOM to set up processes for declaring an event.
- Insurers with over \$10m of GWP across the eligible classes in cyclone-affected areas must join the pool. Insurers with over \$300m of householders' premium in cyclone-affected areas must join by 31 December 2023, while all other insurers must join by 31 December 2024.
- ACCC will monitor prices to determine whether savings are being passed on to policyholders.

10. CYCLONE PREMIUM RATES (source ARPC Website – Finity Actuarial reports – Premium Rate Assessment Report Updated for Consultation as at 1 Oct 2022; and CRP Premium Rate Assessment Report)

Figure 1. Data received for consultation (initial and updated)

Region	Home		Strata		SME	
	Consultation	Initial Rates	Consultation	Initial Rates	Consultation	Initial Rates
SE Qld	329,117	148,141	11,439	140	9,133	48
Northern Qld	132,326	46,126	1,857	189	10,286	141
Rest of Northern Australia	11,174	86	48	72	1,571	47
Lower WA	146,756	65	8,695	68	10,062	35
Northern NSW	101,561	680	2,469	62	3,648	10
Total	720,934	195,098	24,508	531	34,700	281

Figure 2. AAL (initial rates)

	Suggested CRP premium
Wind	710
Fluvial (riverine) flood	74
Storm Surge	49
Total risk premium	833
Insurer claims handling loadings	17
ARPC operational expenses	18
Target Premium Pool	867

Figure 3. CAT models used (source Annual Report 2021/22)

	Wind	Storm Surge	Fluvial Flood	Pluvial Flood
RMS	✓ ¹			✓ ¹
Risk Frontiers	✓ ¹			
COMBUS	✓ ¹	✓ ¹		✓ ¹
Finity Finperils		✓ ²		
Aon CHIP		✓ ²	✓ ²	
JBA			✓ ²	

¹ Probabilistic models

² Deterministic models

Figure 4. Savings (initial rates)

Table 1.3 – Summary of average premium savings by class

Product class	Average savings (sample size)			Total sample size
	All record samples (QLD, NT, WA, Northern NSW)	Northern Australia (CRESTA 5-20)	High premium band in Northern Australia ³	
Home ¹	-8% (194,552)	-19% (45,904)	-38% (451)	194,552
SME ²	-14% (281)	-17% (188)	-28% (5) ⁴	281
Strata	-13% (531)	-15% (261)	-18% (6) ⁴	531

¹Policies with BLD cover, predominantly (99%) QLD policies

²Policies with BLD cover

³Average savings for highest premium bands (>\$1.50 per \$100 SI)

⁴Insufficient data for reliable analysis

Figure 5. Home by area (initial rates)

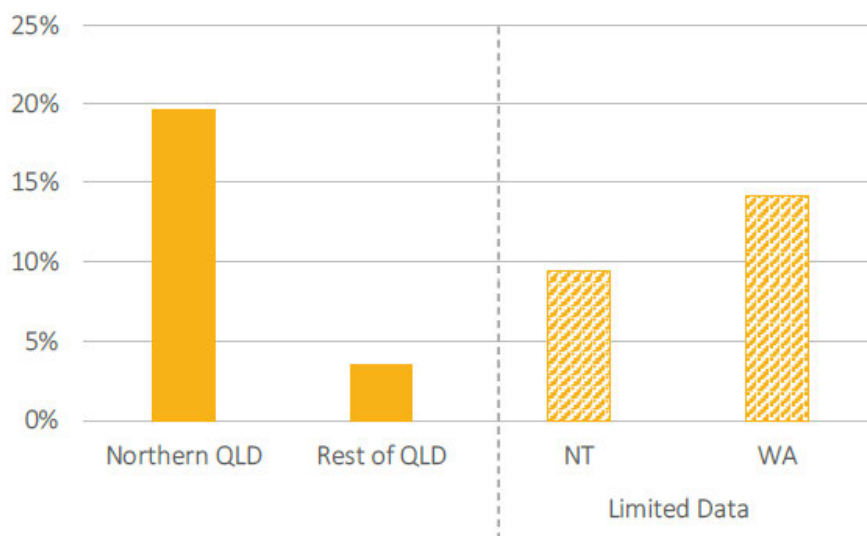


Figure 6. Average Premium Savings

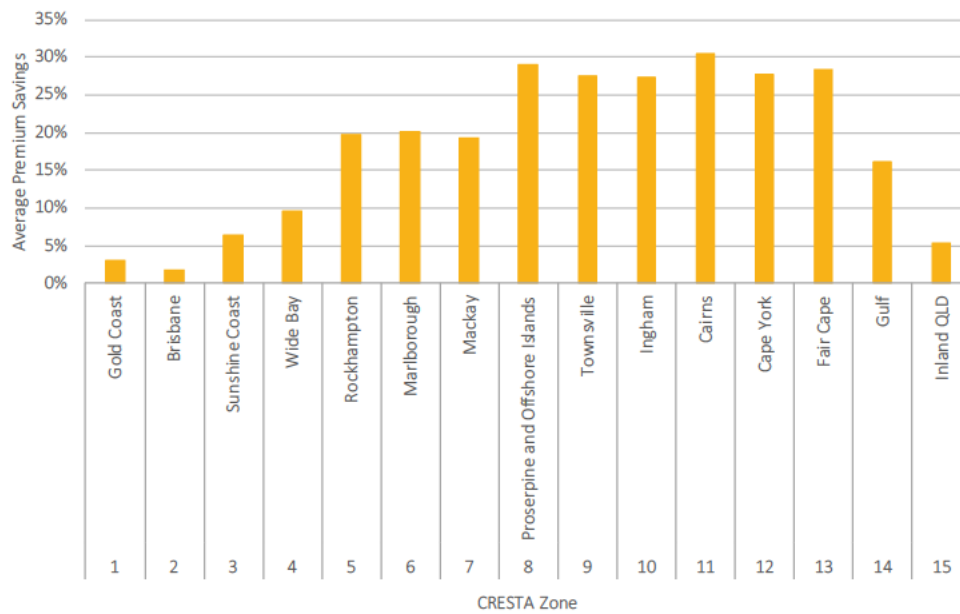


Figure 7. Sample Data – Proportion of Policies in Cyclone affected Areas

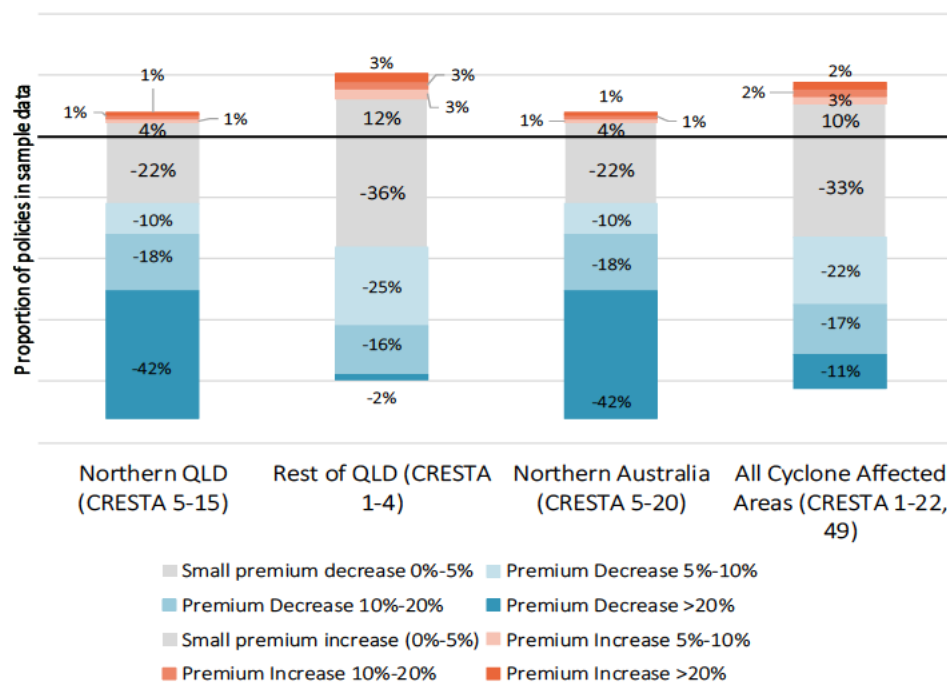


Figure 8. Home by risk band (initial rates)

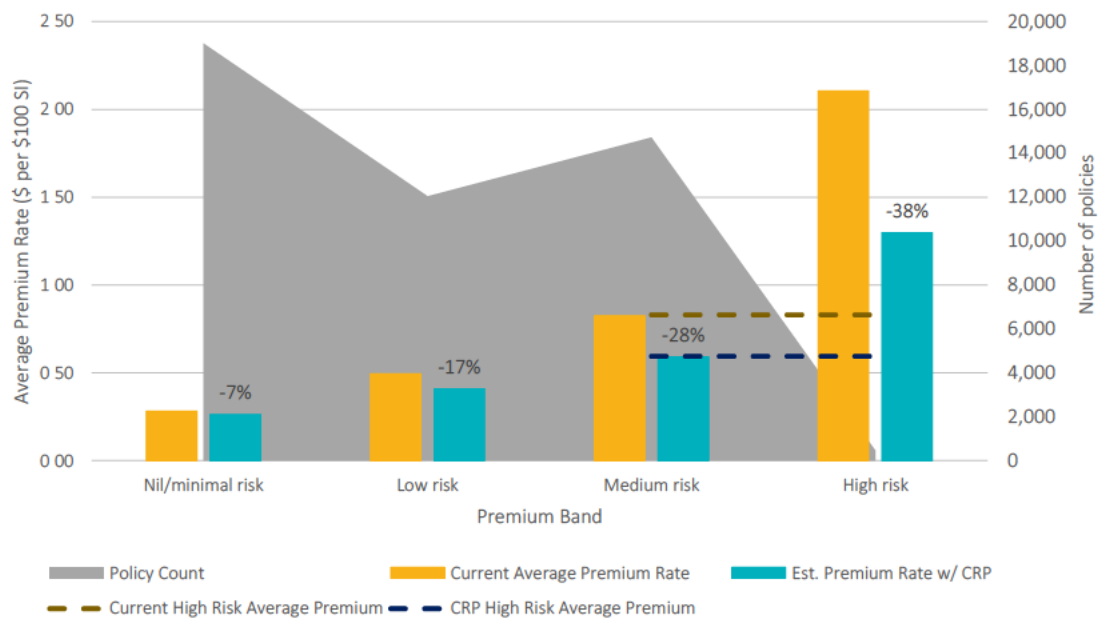


Figure 9. Proportion of Policies – Sample Data

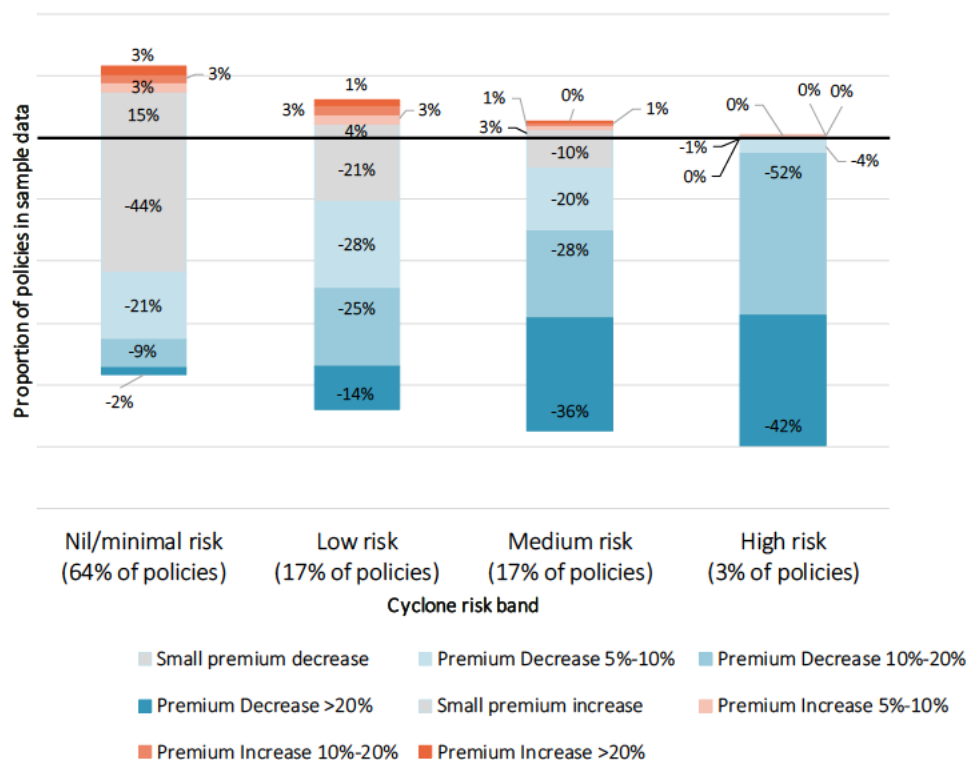


Figure 10. Strata by area (initial rates)

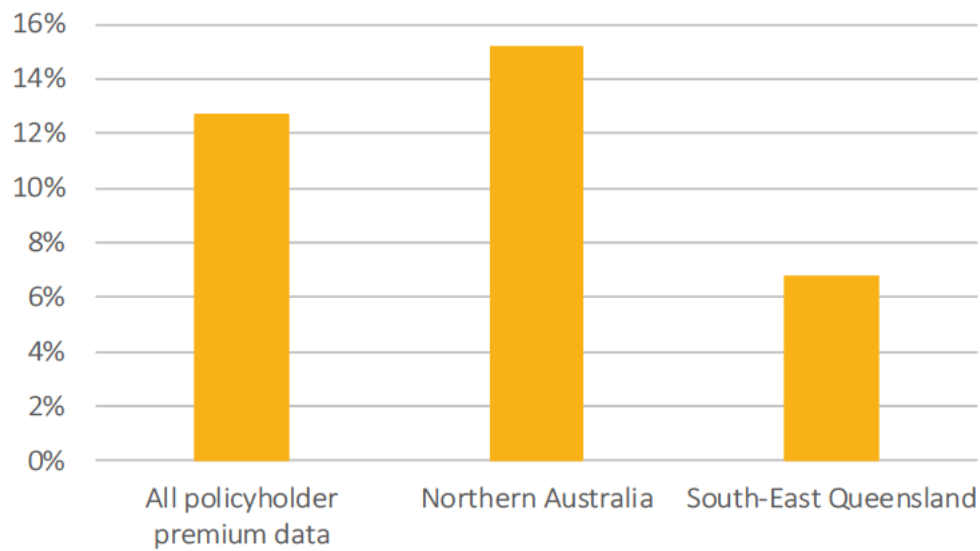


Figure 11. Strata by risk band (initial rates)

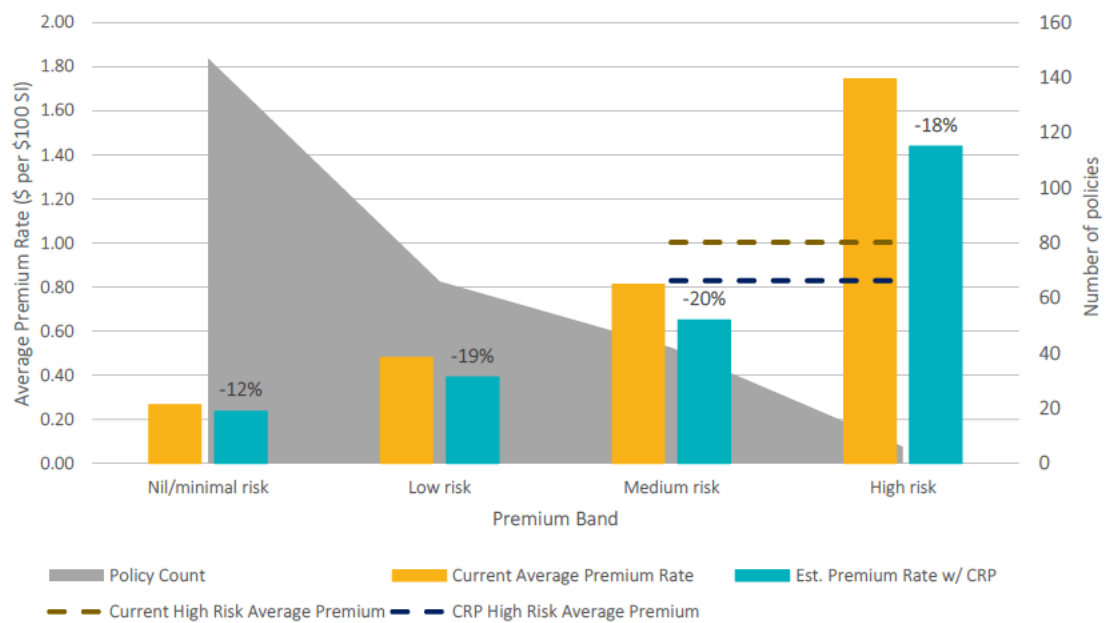


Figure 12. SME by area (initial rates)

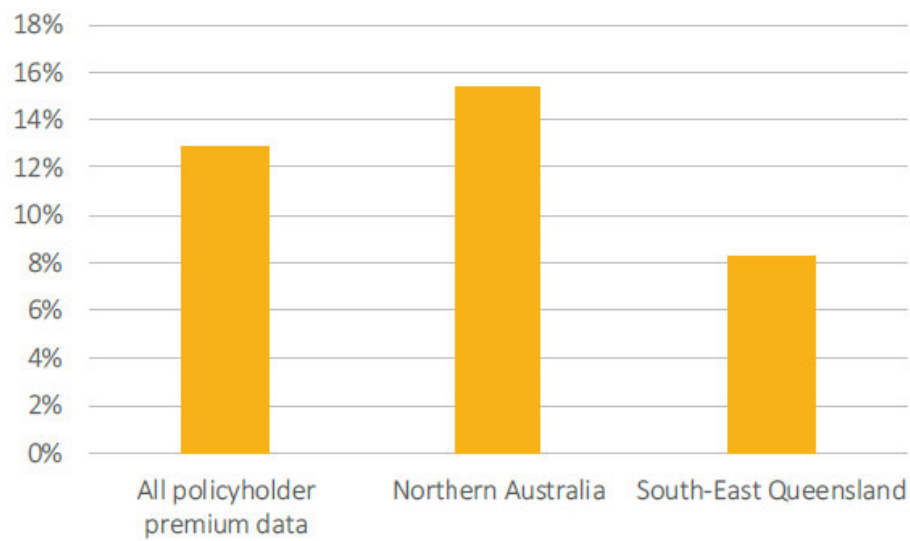


Figure 13. SME by risk band (initial rates)

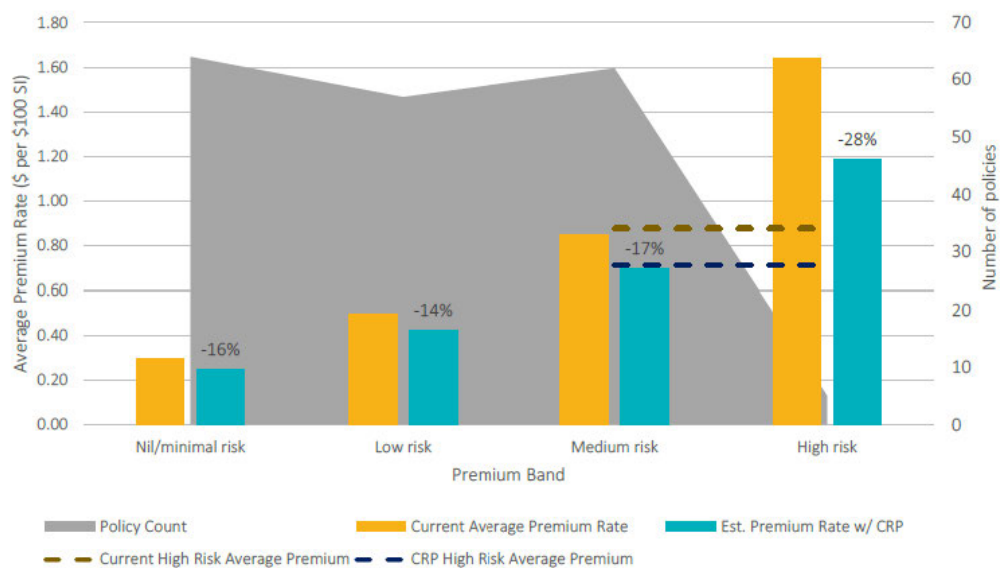


Figure 14. Updated rates – change from initial: Target premium pool

Description of change	Target premium pool (\$m)
Previous estimate of premium pool	867
Revised risk assessment for WA / Pilbara	(45)
Revised cyclone risk for strata buildings	(17)
Non-insurance assumption	(29)
Overall changes	(91)
Revised estimate of premium pool	776

Figure 15. Updated rates – change from initial: Premium collected

Description of change	Estimated premium collected (\$m)
Previous estimate of premium collection	867
Reduced rates for wind bands V and W	(22)
Change wind band allocation for WA suburbs	(19)
Strata	
Sum insured relativity for wind	(6)
Increased discount for new buildings	(1)
Increased discount for concrete	(4)
Number of storeys for wind	(1)
Number of storeys for flood/surge	(4)
Other revisions to the rating formula	(15)
Non-insurance assumption	(19)
Overall changes	(91)
Revised estimate of premium collection	776

Figure 16. AAL (updated rates)

	Suggested CRP premium
Wind	623
Fluvial (riverine) flood	70
Storm Surge	49
Total risk premium	742
Insurer claims handling loadings	16
ARPC operational expenses	18
Target Premium Pool	776

Figure 17. Savings (updated rates)

Table 1.2 – Summary of average premium savings by class (1 October 2022 rates)

Product class	Average savings (sample size)			Total sample size
	All record samples (QLD, NT, WA, Northern NSW)	Northern Australia (CRESTA 5-20)	High <i>total</i> premium band in Northern Australia ²	
Home	-6% (720,934)	-13% (143,500)	-32% (2,416)	720,934
SME ¹	-6% (34,700)	-10% (11,857)	-13% (274)	34,700
Strata	-14% (24,508)	-37% (1,905)	N/A ⁴	24,508

¹Policies with BLD cover

²Highest premium band defined as \$1.50+ per \$100SI for Home and SME

³Cannot be reliably estimated due to data limitations

Figure 18. Home by area (updated rates)

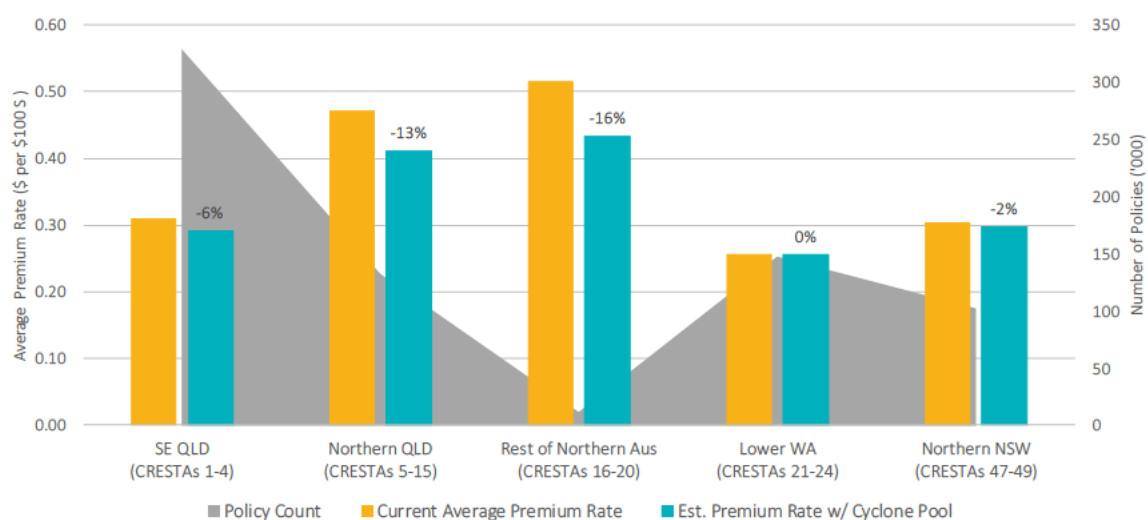


Figure 19. Proportion of Policies

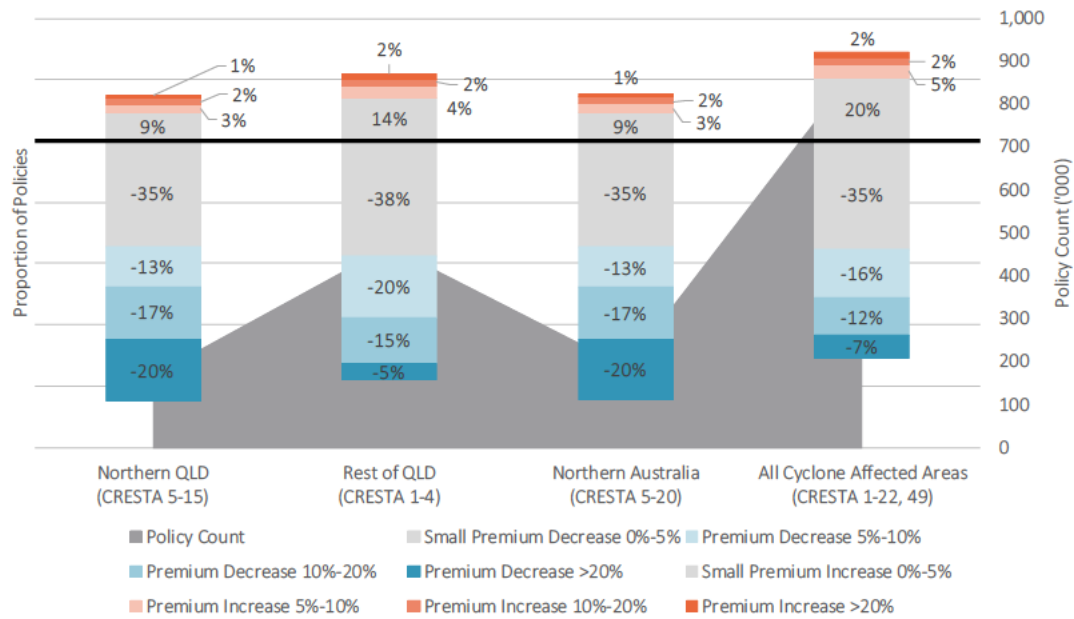


Figure 20. Home by risk band (updated rates)

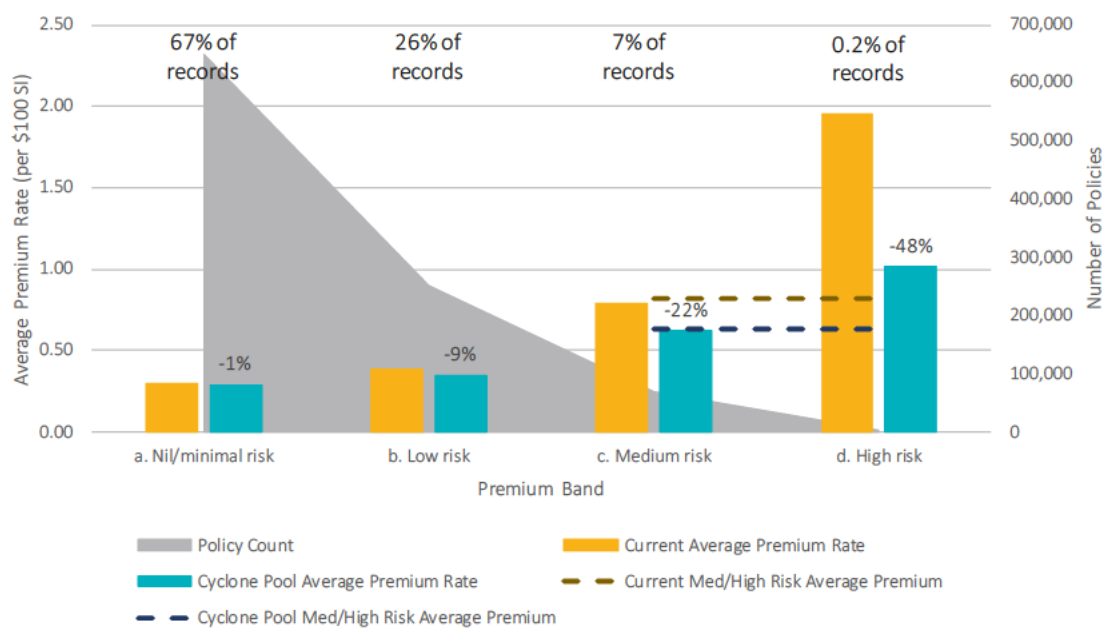


Figure 21. Proportion of Policies in sample data

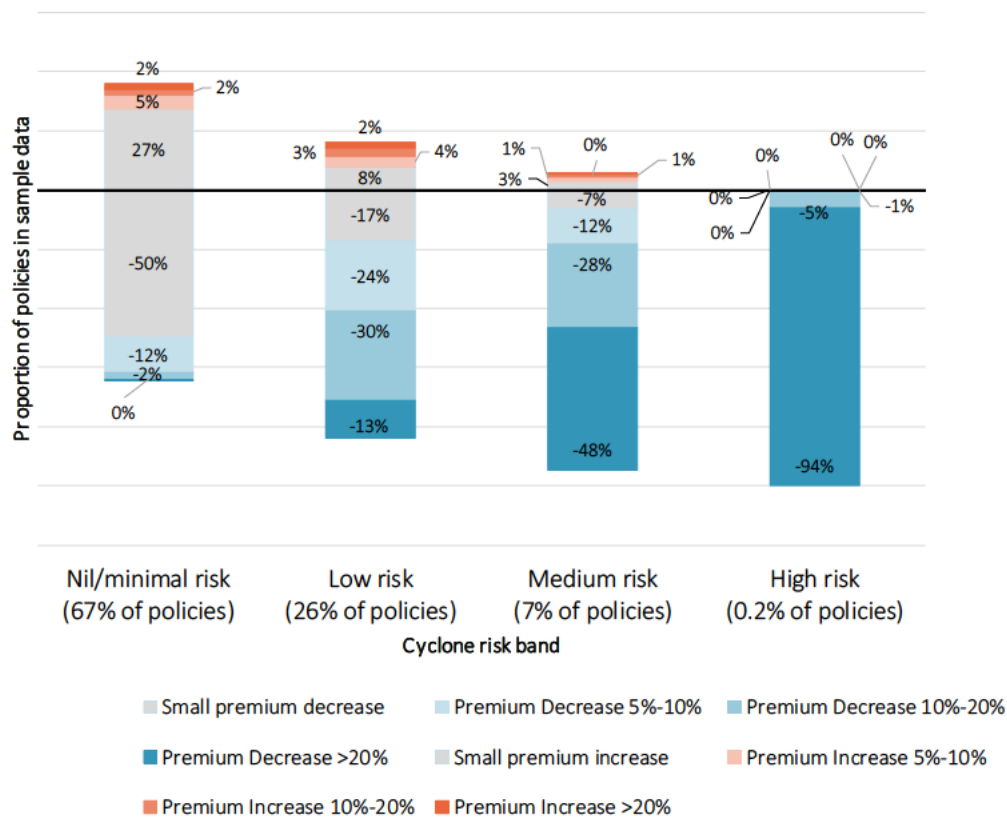


Figure 22. Strata by area (updated rates)

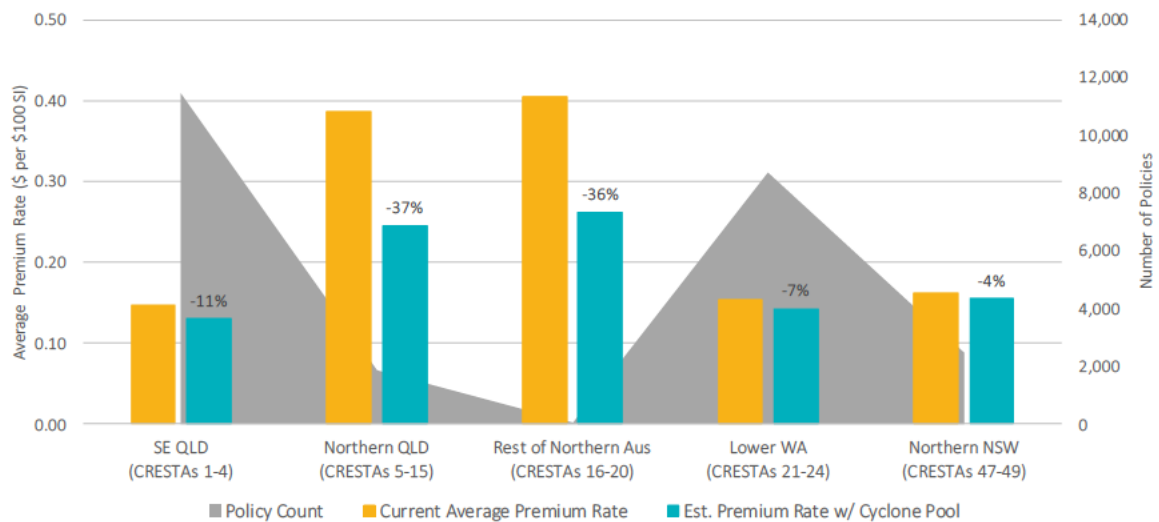


Figure 23. Strata by risk band (updated rates)

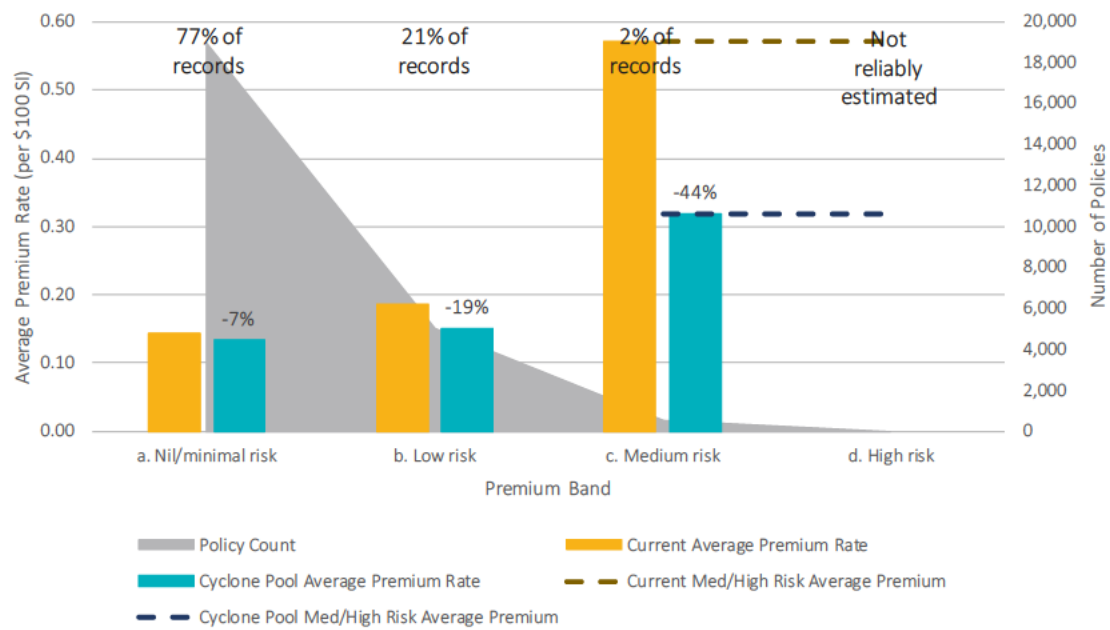


Figure 24. SME by area (updated rates)

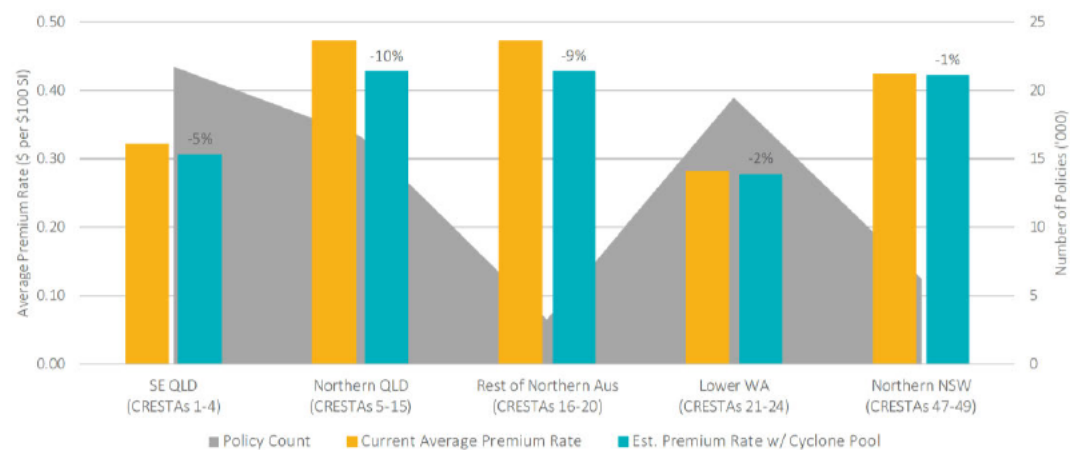


Figure 25. SME by risk band (updated rates)

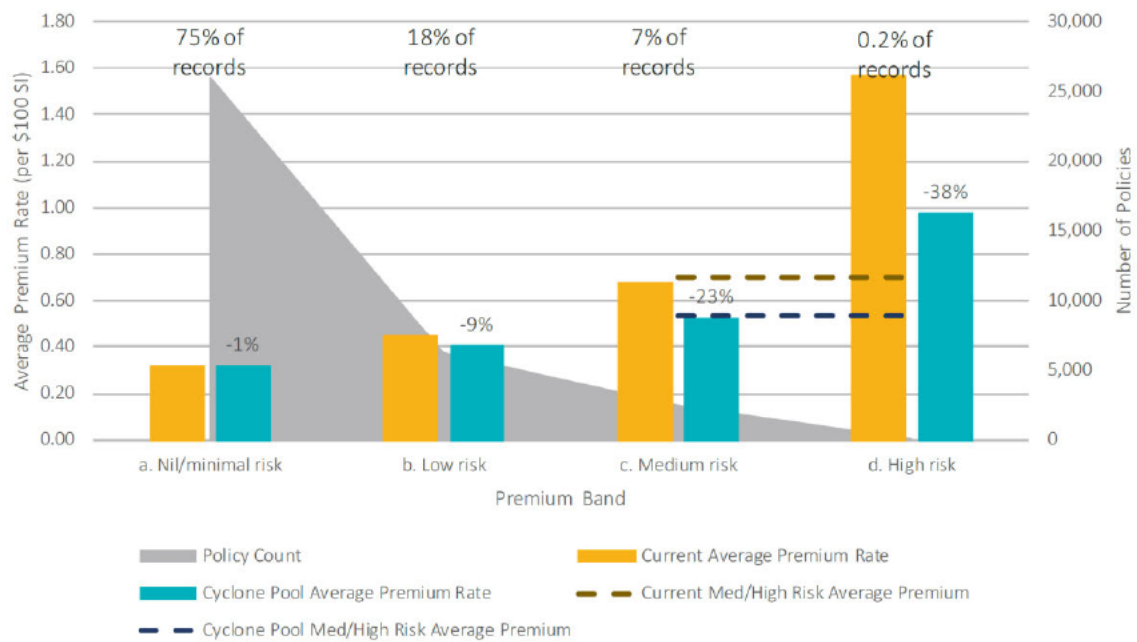
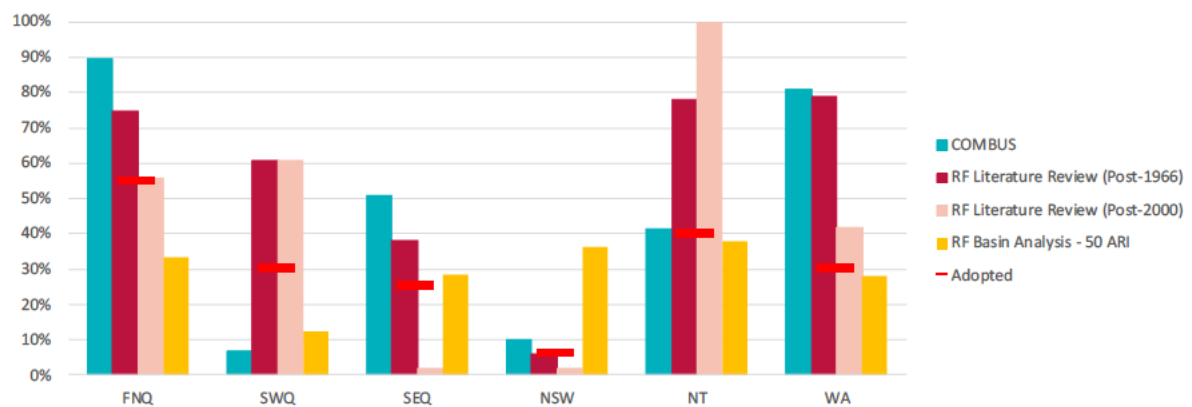


Figure 26. Cyclone related flood proportions



11. **Cyclone Pool Questions and Answers** (*source – As above chapter 10; and ARPC website CRP Flood Analysis Report 30 Jun 2022; and statements of fact*)

- **How have you estimated the cost of cyclone-related flooding?** (*source – unsourced*)
 - To estimate the cost of cyclone-related flooding for the Cyclone Pool we estimated the total cost of riverine (or fluvial) flooding (both overall and insured), then estimated the proportion of flooding attributable to cyclone.
 - We have published a report that is publicly available on our website on how we estimated the proportion of riverine flood attributable to cyclone. This report references two studies conducted by Risk Frontiers, including a literature review of the cost from historical events, and a basin analysis using historical river gauge data.

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- **How did you estimate savings?**
 - ARPC received over 750k individual policy premium records from four leading insurers to inform the October premiums.
 - Insurer cyclone premiums were replaced with cyclone pool premiums and savings were estimated assuming all else remained equal
 - Estimates assume insurers pass on premium savings to policyholders which ACCC has a role in monitoring

- **Why did savings reduce from updated rates?**
 - For each iteration of premiums, the data we have had to work with has become more robust. Between July and October, premium data increased from ~200k records to ~750k records as more insurers provided whole of portfolio data rather than just small samples. This allowed estimates to be more robust.
 - From July to October, whilst pool premium rates decreased across almost all segments, the improved data showed that savings in some areas were lower.
 - In designing the scheme, insurers requested this flexibility to allow smoothing of premium rates for policyholders. There are sufficient savings estimated from the pool to allow insurers to smooth outcomes for policyholders and prevent premium increases.
- **How has ARPC helped to minimise possible premium increases?**
 - We have designed the premium rates to minimize policyholder disruption and the capping of premium rates for high-risk regions will leave to material savings for those under the greatest affordability pressures.
- **Why would ARPC's premiums be higher than the insurers?**
 - It is possible for the pool rates to be higher than an insurer's cyclone rates for some properties due to:
 - Different views on risk – all modelled outcomes that are highly uncertain.
 - Commercial adjustments e.g., discounting, capping/collaring.
 - Specific risk underwriting capturing factors not covered within pricing formula (particularly for large strata).
 - ARPC's rates are more likely to be higher than existing premiums in low-risk areas. In high-risk areas, ARPC has capped cyclone rates, so the incidence of increases is expected to be very small.

- **Are Brisbane rates being increased to cross subsidise and create discounts in north QLD?**
 - That is not the expectation. Savings estimates, based on insurer data, show that the impact of the pool is that premiums in SEQ are comparable to current premiums.
 - Insurer premiums contain margins. In low-risk areas, such as Brisbane, the pool is required to charge comparable premiums. This means the pool collects margins in low-risk areas.
 - In high-risk areas, the pool is required to target lower premiums to high-risk areas. Lower premiums can arise as ARPC is not charging margins for uncertainty or profit. It is also applying the margins collected in low-risk areas to reduce premiums in high-risk areas.
- **Will policyholders still see savings given the hardening market?**
 - The hardening market will obscure the visibility of savings generated by the pool, particularly in low-risk areas.
 - Private market Insurance premiums are increasing due to non-cyclone reasons such as other peril losses over the past few years and increases in building cost inflation.
 - Because policyholders don't see their cyclone premium separately on their policy documents, the savings generated by the pool will be mixed in with effects from non-cyclone impacts. This issue will be most prevalent in low risk areas.
 - The cyclone pool seeks to alleviate affordability issues in Northern Australia where the majority of risk is driven by cyclone.
 - In Northern Australia, the pool is taking almost all cyclone exposure (ground up with unlimited vertical and horizontal coverage) away from the private market and replacing current premiums with subsidised pool premiums.

- Therefore, even though there are going to be increases in many areas due to the hardening market, in Northern Australia where the majority of risk is driven by cyclone and the pool has capped cyclone premiums, it is still expected that the pool will generate savings.
- **How is the pool incentivising mitigation?**
 - Mitigation is the key to delivering affordable coverage given increasing environmental risks in the long run.
 - The pool premium rates provide discounts for home policies for:
 - Window protection
 - Roller door bracing
 - Roof retrofitting or replacement
 - These are the items that have been identified as the most important in reducing property damage from cyclones and are currently asked by some insurers in the market. The cyclone pool is expected to encourage more insurers to ask policyholders about mitigation.
 - ARPC intends to introduce similar measures for SME and Strata in the future. Working alongside experts and engineers to design these.
- **Does the cross subsidisation create incentives to develop in high-risk areas?**
 - This is an important question. Unintendedly encouraging people to put themselves in harm's way is a bad outcome. It would also adversely impact the operation of the pool.
 - In the first instance, the change in the distribution of risks insured by the pool will be monitored in the Financial Outlook Report. If we do see that we are incentivising development in high-risk areas, then the rating for new builds would need to be reviewed. This expect this question would be part of the formal review of the cyclone pool scheduled for 2025. One option would be for the pool to stop any subsidy for new developments in high-risk areas.

- **How have you ensured premium rates are sufficient?**
 - ARPC has undergone a comprehensive process to use market leading models and thoroughly analysed all available data to ensure the pool is meeting policy objectives. Specifically:
 - ARPC has licensed market leading catastrophe models across Wind, Storm Surge and Flood that provide an estimate of total risk cost.
 - Insurer data has been supplemented with external data sources to for a view of the total cyclone pool exposure and run through the cat models.
 - We have ensured that the premium rates in total will collect a premium pool that is sufficient to cover the Average Annual Loss estimated from the catastrophe models plus allowances for insurer claims handling expenses and ARPC's operational expenses.

- **With the decrease in rates after the July – September consultation, are rates still sufficient?**
 - The consultation process afforded ARPC an opportunity to gather additional evidence from insurers and catastrophe modellers about the level of risk the cyclone pool faces.
 - Premium rate decreases were driven by an updated view of the Average Annual Loss, through additional claims data, additional insurer data and cat modelling information from the Verisk catastrophe model.

- **How have you thought about climate change?**
 - Climate change is a key issue we have considered and will continue to be a focus for ARPC going forward.
 - Climate change is expected to impact the frequency, severity, and location of cyclones. However, the specific impact is highly uncertain. The key point is that the risks faced by the pool will change over time. The pool design has settings that provide for the management of changing risks over time.

The approach we have taken is:

- We set the initial premium rates based upon the best available current view of the risk. To develop the cyclone pool premium rates, ARPC procured catastrophe modelling tools which provide credible and widely accepted views of risk (as required by the policy objectives to charge rates comparable to the current market). We did not make an explicit additional adjustment for climate change as the models reflect the best view of current risk and our intent was to provide premium rates appropriate for 2022.
- In future periods, climate change may lead to a different view of the risk. What that will be is highly uncertain. The pool needs to set premiums on a cost neutral basis. We did not load the premium rates for such uncertainty.

Risks might change in the future due to:

- Climate change may increase the overall level of cyclone hazard over time but this does not necessarily increase risk across the board; in fact, some things may decrease (such as overall cyclone frequency or risk in low latitude regions) while other things increase (such as rainfall intensity, severity of higher category events, or risk in mid-latitude locations such as Brisbane or northern NSW). These changes can be monitored through the Financial Outlook report and changes reflected in future premium decisions as they become appropriate.
- Other factors will also change the risk profile of the pool. The pool will incentivise mitigation through premium savings and this will hopefully make housing stock more resilient to cyclone risk over time.

Financial Outlook Report:

- As required under the Act, ARPC will publish an annual financial outlook Report. The Financial Outlook Report will comment on the adequacy of the premium rates and consider the ongoing impacts of climate change on ARPC's exposure. ARPC will review its premium rates annually and will

reflect the evolving scientific understanding of the impact of climate change within its annual premium rate reviews.

- **How has high market inflation been considered in the premium rates?**

- The cyclone pool premiums are rates per sum insured
- Over the long term, inflation in construction costs and building materials should be fully reflected in sum insureds and hence no explicit adjustment to the premium rates for inflation will be required.
- In the short term there is likely to be a lag where sum insureds don't increase by the same rate as inflation.
 - One benefit of the pool is that it is seeking to price over the long term and doesn't need to adjust premium rates for shorter term influences.
 - However, the catastrophe models have been run with an explicit 5% allowance for underinsurance to make some allowance for the expectation that sum insureds will be lower than replacement costs.
- We recognise the disruption caused by inflation in the economy will need to be revisited in 2023.

- **Would the pool work for flood?**

- The current pool design is fit for purpose for cyclone.
- Each peril has its own characteristics and the nature of risk for flood is different to cyclone. The flood risk is more acute and there isn't the same capacity for margins on low-risk properties to be re-allocated to high-risk properties.
- A pool could be designed that would produce savings for flood but would require a different design to the cyclone pool.

- **Do you think the pool should include all flood and bushfire?**

- This is not an area we have done any detailed work. Focus has been on implementing the cyclone pool as defined in the legislation.

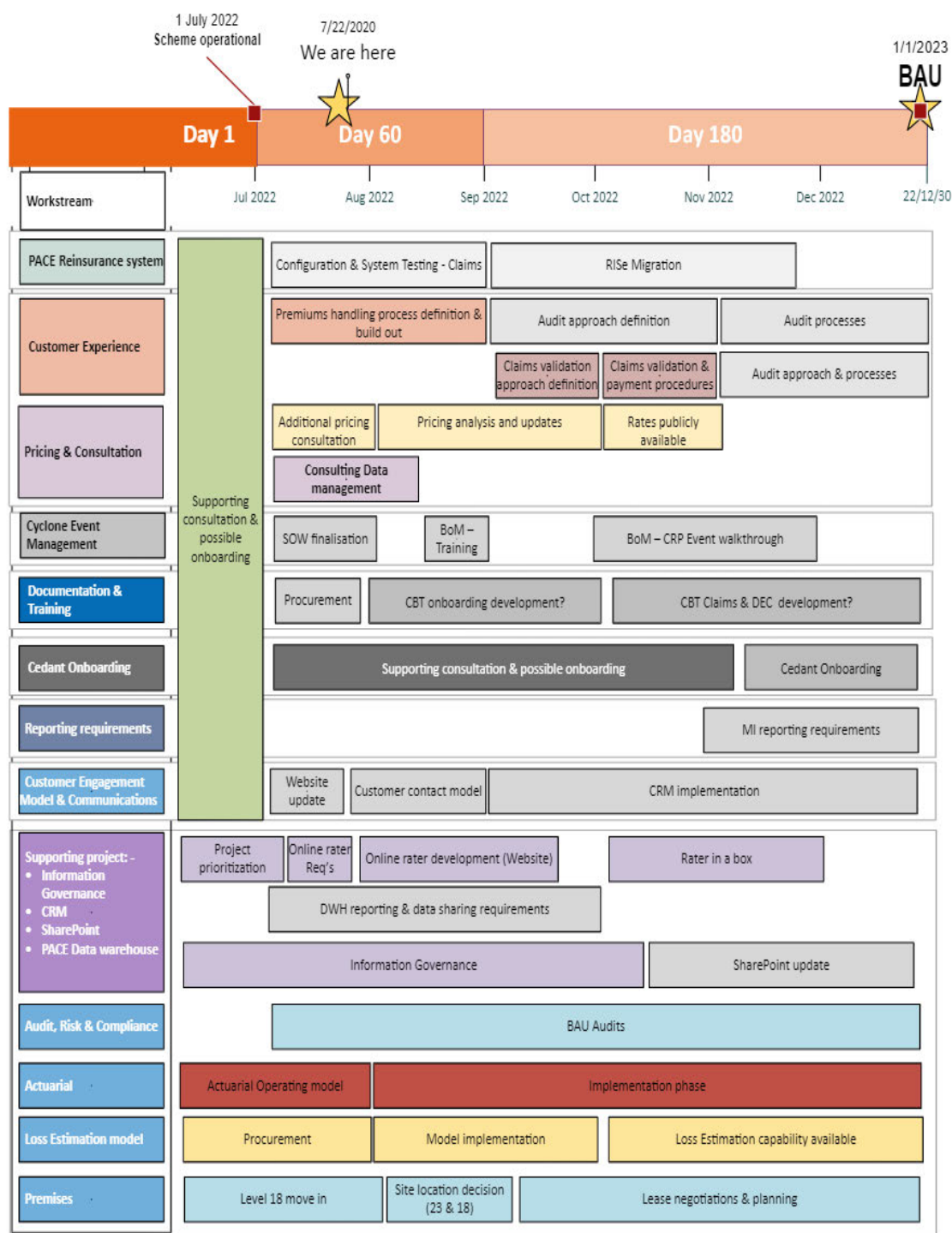
12. **CYCLONE REINSURANCE AGREEMENT** (*source – statement of fact*)

ARPC developed the cyclone reinsurance contract:

- In conjunction with Clayton Utz (CU) (external Legal) and The Australian Government Solicitors (AGS) office.
- ARPC produced a draft Reinsurance Agreement by first comparing a standard market catastrophe reinsurance agreement and tailoring the agreement to meet the legislative requirements of the Pool.
- The first draft was circulated to various insurance companies where ARPC requested feedback (early February 2022).
- Meetings were held with the various insurers to discuss the feedback (early to mid-February 2022).
- Where feedback was seen to enhance the quality of the agreement it was incorporated (signed off by CU and AGS).
- The second draft of the reinsurance agreement was circulated on 30th June 2022 when the Cyclone Premium rates were published (30 June).
- Between 30 June and 1 October 2022:
 - insurers provided some additional feedback in the form of written submissions. Where the feedback was seen to enhance the quality of the agreement the changes were adopted (signed off by CU and AGS)
 - ARPC amended the Reinsurance Agreement to accommodate some minor changes relating to Lloyd's syndicates.
- The Final Agreement was released along with the Cyclone Rate 1 October 2022.
- The Final Agreement is published on the ARPC website.

13. CYCLONE POOL IMPLEMENTATION GANTT CHART

(source – internal document)



14. STAKEHOLDER ENGAGEMENT *(source Annual Report 2021/22)*

14.1 INSURERS

- During 2021-22, ARPC remained committed to developing and sustaining key stakeholder relationships through timely, open communication, understanding their needs and expectations, and delivering value.
- ARPC held regular meetings with insurers, major commercial property owners, relevant state and Australian Government agencies, and industry associations and advised insurer customers on Reinsurance Agreements and insurer premium submissions.
- For cyclone, ARPC worked extensively with insurance industry stakeholders to:
 - develop the new cyclone pool reinsurance agreement
 - develop premium rates, with input from our consulting actuaries, key industry stakeholders, and The Treasury, with the initial premium rates and summary of actuarial modelling published on 28 June 2022.
 - Consultation meetings have been conducted between February 2022 to current date.
- Other stakeholder activities included
 - Insurance market briefing on the 2022 terrorism retrocession program
 - Annual Terrorism Risk & Insurance Seminar - in person & livestreamed
 - Networking function in Sydney
 - Insurer customer review program
 - Quarterly newsletter, Under the Cover
 - LinkedIn posts, website updates and articles in industry publications.

14.2 COMMUNITY

- ARPC has engaged with stakeholder groups such as the Local Government Association of Queensland during August and October 2022 in relation to the cyclone pool.
- ARPC also engaged with ReachOut through a sponsorship partnership commencing in July 2021 for a period of 2 years. This is a social engagement project to reduce the risk of youth engaging in anti-social behaviours that could result in violent extremism.

14.3 GOVERNMENT

- ARPC has worked closely with other government agencies to establish the pool including:
 - The Treasury's Cyclone Reinsurance Pool Taskforce
 - Australian Competition and Consumer Commission (ACCC)
 - Australian Government Actuary (AGA)
 - Australian Government Solicitor (AGS)
 - Australian Prudential Regulatory Authority (APRA)
 - Bureau of Meteorology.

15. CLAIMS *(source Annual Report 2021/22)*

- No claims have been paid against the terrorism reinsurance pool.
- No claims for cyclone as ARPC have not onboarded insurers at this point.
- If there is a cyclone declared during the upcoming season, ARPC will declare the event (via notifiable instrument), however no claims will be received or processed as there are currently no insurer customers.

16. BUREAU OF METEOROLOGY *(source Annual Report 2021/22)*

- ARPC has partnered with BoM to develop Declared Cyclone Event (DCE) procedures as follows:
 - The BoM will notify ARPC within 24 hours of its observation with the relevant date and time of a start, re-intensification, and end of a named cyclone likely to impact Australia.
 - On receipt of the BoM notification and within 24 hours, ARPC is required to make a declaration, via notifiable instrument of the start, re-intensification and/ or end of a cyclone on its website. The DCE must include:
 - Relevant start and end times
 - The claims period start and end times for the cyclone, noting the claims period for eligible losses is within 48 hours after the cyclone's declared end.
 - Insurers will continue to pay cyclone-related claims as per the terms and conditions of individual insurer' policies. Consumer claims with loss dates outside of the declared cyclone pool claims period will stay covered by insurers as per their underlying Product Disclosure Statements (PDS).
- ARPC and BoM signed the formal agreement and side letter on 2 November 2022.
- ARPC has subscribed to Early Warning Network (EWN) to assist with Cyclone Forecasting, Tracking, Alerting & Reporting – EWN provide these services to a range of companies across a broad range of industries including the insurers.