Chapter 2

The Australian states' current insurance and reinsurance arrangements

2.1 The terms of reference for this inquiry direct the committee to examine—among other matters—the current insurance and reinsurance arrangements of the states and territories of their assets and infrastructure. This chapter considers these matters.

Captive insurance and reinsurance

2.2 All Australian states and territories have a captive insurer, which are state agencies established with the specific objective of financing risks to state government assets from public and products liability and special industrial risks (including disasters). Covered agencies pay premiums to the captive insurer, which then pays to replace public assets when needed.

2.3 Reinsurance is insurance that is purchased by an organisation to transfer the risk of claims where its own balance sheet is unable to meet potential claims. Reinsurance is therefore a risk sharing arrangement, whereby the insurer obtains cover from a third party (the reinsurer) for part of the credit risks that it has guaranteed, in exchange for the payment of a premium.

State governments' captive insurance and reinsurance arrangements

2.4 In the first instance, the committee notes the lack of transparency in states' reinsurance arrangements. The committee has not received, nor has it found, a publicly available list of the Australian states' and territories' reinsurance arrangements. As this chapter attests, the state governments' websites and annual reports are of varying quality. And, as subsequent chapters of this report note, even the Commonwealth Grants Commission—which adjusts states' GST share on the assumption that all states have the same spending policies in regard to natural disaster relief[1]—seems to be without a clear picture of these insurance costs.[2]

2.5 Most Australian state governments have reinsurance for their assets paid through premiums to international insurance companies. Queensland appears to be the only mainland state that does not have external reinsurance arrangements.[3]

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1 Commonwealth Grants Commission, *Submission 1*, p. 1.

2 Mr John Spasojevic, Secretary, Commonwealth Grants Commission, *Proof Committee Hansard*, 13 May 2011, p. 14.

3 Mr John Tsouroutis, *Correspondence to the committee*, 6 May 2011, p. 1.

2.6 Among the states that do have external reinsurance arrangements, the level of cover varies. The committee is aware that Victoria has reinsurance for its roads, for example.

Queensland

2.7 The Queensland Government Insurance Fund (QGIF) is the Queensland Government's captive insurer. The QGIF commenced operation on 1 July 2001 and is a managed fund within the general government sector. Agencies pay premiums to QGIF, claims are met from it, and reserves are built up to meet the cost of insurable liabilities.[4]

2.8 As mentioned, the Queensland Government does not purchase reinsurance for QGIF on the global market. Instead, the state government is heavily reliant on funding its natural disaster relief costs through arrangements with the Commonwealth. The Queensland Government's website states that the purchase of reinsurance as appropriate to the management of major and catastrophic risks 'is an ongoing consideration'.[5]

2.9 The committee found it difficult to identify the QGIF's current financial position. There is very little detail on the Fund's activities in Queensland Treasury's Annual Reports or on the QGIF website.

2.10 The committee has seen a note sent from the Queensland Treasury to the Queensland Treasurer on 21 January 2011. The note was obtained by *The Australian* newspaper on 11 April 2011 under the State's *Right to Information Act 2009*. It shows that the QGIF's premium revenue for 2010–2011 was $113 million, comprising health litigation ($57 million), general liability (28.4 million) and property ($24.1 million). Queensland Treasury's 2009–10 Annual Report lists the QGIF's claims and concessions at $110 million.[6]

2.11 In his précis for the committee on the Queensland Government's correspondence (see chapter 1), Mr Tsouroutis noted that as of 30 June 2010, the QGIF had $685.5 million in outstanding insurance liabilities. In February 2011, the Queensland Treasurer stated that the Fund has more than $700 million in reserves. Mr Tsouroutis concluded that:

> In the absence of reinsurance, it appears that the QGIF had negligible net reserves to meet any significant net claims such as those which arose from

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4 Queensland Government Insurance Fund, http://www.qgif.qld.gov.au/contents/operational_structure.shtml (accessed 18 April 2011).

5 Queensland Government Insurance Fund, http://www.qgif.qld.gov.au/contents/operational_structure.shtml (accessed 18 April 2011).

6 Queensland Treasury, *Annual Report 2009–10*, p. 93. http://www.treasury.qld.gov.au/knowledge/docs/annual-reports/2009-10/pdf/docs/complete-treasury-annual-report-2009-10.pdf (accessed 23 June 2011).

> the 2011 natural disasters, after allowing for its current fund reserves which essentially only covered its current outstanding liabilities, prior to the 2011 natural disasters.[7]

Victoria

2.12 The Victorian Government underwrites the state's exposures through its captive insurer, the Victorian Managed Insurance Authority (VMIA). The VMIA's insurance covers major government assets and infrastructure, the public healthcare system and community service organisations. The Chief Executive Officer of the VMIA, Mr Stephen Marshall, explained to the committee that the Authority's objective is to protect its balance sheet and the state's balance sheet with regard to losses incurred as a result of disasters.[8]

2.13 The VMIA's portfolio represents just over $108 billion in insured assets, with annual premium revenue in 2009–2010 of nearly $175 million.[9] The same financial year, the Authority paid an annual insurance premium of $36.2 million, leaving net premium revenue of $138.8 million.[10]

Table 2.1: Victorian Managed Insurance Authority's reinsurance

	2010 ($'000)
Premium revenue	*$174,935*
Outward reinsurance premium expense	*$36,179*
Net premium revenue	*$138,756*

Source: *VMIA Annual Report 2010*, p. 12.

2.14 The VMIA has a policy of purchasing reinsurance to limit the State's financial exposure to recovery from natural disasters. In 2009–2010, this included $1.45 billion for industrial special risks. The VMIA informed the committee that in 2010–2011, the state has industrial special risk insurance for $2.05 billion worth of assets within the state.[11] The VMIA retains the first $50 million for each event and reinsures the remainder in the local and overseas insurance markets.[12]

2.15 In addition to special industrial risks, the VMIA also has public and products liability insurance which includes cover for the state's bridges and roads. Again, the

7 Mr John Tsouroutis, *Correspondence to committee*, 6 May 2011, p. 3.

8 Mr Stephen Marshall, *Proof Committee Hansard*, 13 May 2011, p. 25.

9 VMIA, *Annual Report 2010*, p. 6.

10 VMIA *Annual Report 2010*, p. 12.

11 Mr Stephen Marshall, *Proof Committee Hansard*, 13 May 2011, p. 22.

12 Mr Stephen Marshall, *Proof Committee Hansard*, 13 May 2011, p. 22.

VMIA retains the first $50 million for each event and reinsures a further $700 million on the local and overseas reinsurance markets.[13]

2.16 In evidence to the committee, Mr Marshall explained the process for insuring the state's roads as follows:

> VicRoads identify what the replacement value is per kilometre of road, whether it be a single road, single lane, dual highway and the like. VicRoads actually do have quite a robust asset replacement value—I think it is in excess of $20 billion. As I mentioned before, we rely on their valuations in regard to the kilometre of road depending on each of those constructions.[14]

2.17 The Victorian Government is reportedly in talks with the insurer Swiss Re to expand its external insurance coverage. These discussions were initiated by the state government in response to the Black Saturday bushfires.[15] Mr Marshall told the committee that losses of state assets from the 2010 bushfires were 'somewhere between $50 million and $60 million', paid for by the VMIA, 'with very marginal reinsurance recoveries'.[16]

South Australia

2.18 One of the roles of the South Australian Government Financing Authority (SAFA) is as a captive insurer for the Government of South Australia. The 2009–2010 SAFA Annual Report states that although the South Australian Government is fundamentally a self-insurer of most of its own risks, 'it has been considered appropriate and desirable that the state's finances be protected against the financial consequences of a catastrophic event'.[17] The SAFA Annual Report notes that under the Catastrophic Reinsurance program, the items in Table 2.2 are insured at the corresponding levels.

Table 2.2: South Australian Government's insurance and reinsurance 2009–2010

	2009–10 ($m)
Premium revenue	35
Reinsurance expense	7
Net claims	10.3

Source: *SAICORP Annual Report 2009–10*

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13 Mr Stephen Marshall, *Proof Committee Hansard*, 13 May 2011, p. 22.

14 Mr Stephen Marshall, *Proof Committee Hansard*, 13 May 2011, p. 26. Roads at a local government level are insured through the Municipal Association of Victoria.

15 'Victorian Government in insurance talks with Swiss', www.insurancenews.com.au , 4 April 2011.

16 Mr Stephen Marshall, *Proof Committee Hansard*, 13 May 2011, p. 27.

17 South Australian Government Financing Authority, *Annual report 2009–2010,* p. 17.

New South Wales

2.19 The committee has not received information during this inquiry on the insurance and reinsurance arrangements of New South Wales (NSW) Government assets. It is aware that the state's captive insurer is the Treasury Managed Fund (TMF), which provides a full range of insurance covers and services for all participating Agencies.[18] The TMF's website describes its overall purpose as 'to provide structure and services that will assist Agencies in reducing the impact of risk exposures and maximise resources available to support their core business'.[19] The TMF is itself administered by the NSW Self Insurance Corporation (SICorp).

2.20 There is little information on the SICorp website about reinsurance arrangements. It does note that the TMF is protected by 'a comprehensive reinsurance program' and that the TMF has a reinsurance contract with Aon Benfield (Australia) Limited from 1 October 2009 to 30 September 2013.[20]

Western Australia

2.21 The Western Australian Government's self insurer is the Riskcover Fund. The Fund is underwritten by the Crown and is managed by the Insurance Commission of Western Australia on behalf of the state government. As part of RiskCover's commercial claims management service, a whole of State response is provided in respect of Western Australian government risks, to catastrophic losses such as cyclones, bush fires and floods.[21]

2.22 The Riskcover Fund's Statement of Comprehensive Income for the financial year ending 30 June 2010 listed outward reinsurance premium expense at $14.1 million.[22] Again, publicly available data on reinsurance arrangements is difficult to find.

Tasmania

2.23 The Tasmanian Risk Management Fund is the Tasmanian Government's self-insurance fund through which various agencies are covered for personal injury, legal liability, property and travel. The Fund operates on a cost-recovery basis with all

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18 New South Wales Government, 'Treasury Managed Fund', http://www.treasury.nsw.gov.au/insure/tmf (accessed 20 June 2011).

19 New South Wales Government, 'Treasury Managed Fund', website.

20 Treasury Managed Fund, 'Contracts and Tenders', https://riskinsite.nsw.gov.au/portal/server.pt/community/treasury_managed_fund/268/contract___tenders/1288 (accessed 23 June 2011).

21 Riskcover Fund, *2010 Riskcover Fund report*, p. 2.

22 Riskcover Fund, *2010 Riskcover Fund report*, p. 19 http://www.riskcover.wa.gov.au/publications/rc/fund_report/fund_report_10.pdf (accessed 23 June 2010).

participating agencies paying annual contributions to meet claim costs up to $5 million, administrative expenses, and where applicable, insurance premiums and reinsurance costs. The level of agencies' contributions is determined by an independent actuary and reflects their risk exposure, claims experience and nominated excess amounts.[23]

2.24 In setting agency contributions, the Fund aims to achieve: the collection of sufficient moneys each year to fund claims costs and alleviate the financial impact of large unexpected events; equity for user agencies with minimal cross-subsidisation; stability in contributions over time; and incentives for risk management, through recognition of claims experience. The Fund's finances are managed through the Tasmanian State Service Risk Management Account in the Special Deposits and Trust Fund.[24]

Concluding comment

2.25 The committee notes the lack of detailed, publicly available information on the states' and territories' current insurance and reinsurance arrangements. With the exception of Victoria, the collation and publication of this information among the mainland state governments is particularly poor. Chapter 5 makes a recommendation to address this problem.

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23 Tasmanian Department of Treasury and Finance, Tasmanian Risk Management Fund, *Annual Report 2009–2010*, p. 7 http://www.tenders.tas.gov.au/domino/dtf/dtf.nsf/a6c28ced64705388ca256f0700810896/a62275d1cc3569b0ca2577e50082288b/$FILE/TRMF-2009-10-AR.pdf

24 Tasmanian Department of Treasury and Finance, Tasmanian Risk Management Fund, *Annual Report 2009–2010*, p. 7 http://www.tenders.tas.gov.au/domino/dtf/dtf.nsf/a6c28ced64705388ca256f0700810896/a62275d1cc3569b0ca2577e50082288b/$FILE/TRMF-2009-10-AR.pdf