

Minority report by Independent Senator Nick Xenophon

1.1 The natural disasters in Queensland earlier this year have brought into sharp focus both the disaster insurance arrangements of the state and territory governments and the system through which the Commonwealth directs disaster relief payments to the states. These issues were magnified given that the Queensland government is the only major state government without a reinsurance policy for its assets. As *The Australian* reported in March this year:

Unlike NSW, Victoria, South Australia and Western Australia—whose governments pay millions of dollars in premiums a year to international insurance companies to protect their infrastructure—Queensland relies on a deal struck with the Commonwealth to pick up 75 per cent of the recovery costs after a catastrophe.¹

1.2 Even more concerning is that the Queensland government has in the past been offered quotes to reinsure its assets, but declined. In 2000, it received an indicative quote; in 2003–04, a formal quote; and in 2009, there was a review of the state's arrangements but no approach to market. Only now, after the floods and Cyclone Yasi, has the Queensland government returned to the international reinsurance market to seek a quote.

Requests for documentation

1.3 A key aspect of this inquiry has been the committee's request that the Queensland government provide:

...any correspondence, and any related documents, between the Queensland Government and any insurance advisers, insurance brokers, reinsurance brokers, insurers and reinsurers in relation to providing services or insurance products, or offers or proposals of insurance or reinsurance of Queensland Government assets, from 1 January 2000.

1.4 The Queensland government has provided information to the committee in two tranches. First, it provided the committee with several hundred pages of documentation described as 'all non cabinet-in-confidence reinsurance records retained from the requested period'.² The Queensland Government requested that this information be kept confidential.

1.5 Within this documentation, there was an excessive amount of information on aviation reinsurance which is of little or no significance to the broader issue of the

1 Lauren Wilson, 'State goes it alone in shunning insurance', *The Australian*, 2 March 2011.

2 The Hon. Rachel Nolan, Letter to Chair of the Senate Economics References Committee, 9 August 2011.

state's catastrophe insurance and funding arrangements. The documents did note that in 2003–2004, the Queensland government was offered a reinsurance quote. However, this was not purchased.

1.6 Second, and on request, the Queensland government provided a copy of a November 2000 International Risk Management Group (IRMG) report. IRMG was commissioned to provide a feasibility study to assist the Queensland Treasury to provide a centralised insurance scheme to provide property and liability coverage to state government departments. Again, the state government requested that this document be kept confidential. It rejected the committee's request to make the report public stating:

[G]iven that the Queensland Government is currently out to market seeking a quote to insure its assets against future natural disasters, the IRMG report remains commercial-in-confidence and it would not be appropriate for it to be quoted in a direct manner.³

This is despite the report being more than a decade old and only providing indications of what insurance should have cost, rather than actual quotes.

1.7 The committee was also advised that the IRMG report had been provided "in good faith" and Minister for Finance and the Arts, the Hon. Rachel Nolan, suggested that I was "not content with 11 years worth of records".⁴

1.8 In a letter to the Chair dated 16 August 2011⁵, I further contended that it seemed there were two critical documents that were missing from the material that had been provided to the Inquiry by the Queensland government.

1.9 A document prepared by risk managers for Queensland Treasury made reference to 'critical tasks requiring completion' including a 'critical task' to "Finalise Reinsurance coverage for all risks" by 31 May 2001.

1.10 Presumably there ought to be documents relating to the critical tasks referred to, as well as Minutes of meetings by the Queensland Government Insurance Fund Advisory Board in considering this.

1.11 The Chair again contacted the Queensland government to request the release of any relevant documents published during this timeframe, however was advised on 31 August 2011 by the Hon. Rachel Nolan that "there [were] no further documents relating to this request."⁶ It seems extraordinary that the request for the documents

3 The Hon. Rachel Nolan, Letter to Chair of the Senate Economics References Committee, 9 August 2011.

4 Ibid

5 Senator Nick Xenophon, Letter to Chair of the Senate Economics References Committee, 16 August 2011

6 The Hon. Rachel Nolan, Letter to Chair of the Senate Economics References Committee, 31 August 2011.

sought in 1.10 was met with this response. It may well be that the issue of what documents exist will only be satisfactorily resolved following FOI requests of the Queensland government.

1.12 I contend that the refusal of the Queensland government's to release these documents has limited the committee's abilities to exhaustively assess this issue, and one has to question the real impetus behind its refusal to release information that is over ten years old and does not contain actual quotes for insurance.

1.13 I remain of the belief that in 2000, the Queensland government was offered natural disaster insurance that included roads for a premium of less than \$50 million. It is disappointing that the Queensland government has not been forthcoming with this information. Had the Queensland government acted prudentially and reasonably at the time, there would not have been the need for significant Natural Disaster Relief and Recovery Arrangements (NDRRA) payments that taxpayers now face.

The 2003–2004 reinsurance quote

1.14 As noted above, the Queensland government received a reinsurance quote in 2003–2004. The Minister for Finance and the Arts, the Hon. Rachel Nolan, described this policy as the equivalent of an offer to insure a \$500 000 house for \$6400 per year, with no claim being possible without a \$20 000 excess.⁷ However, private insurers and other state governments have been able to purchase reinsurance of \$3 to \$5 billion. Further, the \$20 million excess is not significant because this is typically what a private property insurance fund would meet from its reserves, with claims above this amount being met by the reinsurers.

1.15 The key question, however, is whether the Queensland government could afford *not* to have reinsurance. In the absence of its own reinsurance scheme, the state government has for many years relied on the NDRRA. All other states and territories have their own reinsurance arrangements. I would argue that one \$500 million uninsured catastrophe represents 78 years of insurance premiums at 6.4 million per annum and peace of mind.

The NDRRA

1.16 I contend that the Queensland government's rejection of several reinsurance offers over more than a decade reflects the 'moral hazard' problem identified in the majority report. The Queensland government has had no incentive to insure its assets adequately given the generosity of Commonwealth payments under the NDRRA. However, a key principle of the comprehensively re-drafted 2011 NDRRA (as a consequence of negotiations I had with the Commonwealth government) is that it

7 The Hon. Rachel Nolan, Letter to Chair of the Senate Economics References Committee, 18 April 2011.

should not supplant the states' own reinsurance. If it can be shown that the Queensland government did not adequately insure on the basis of reliance on the NDRRA, then it could be in contravention of the NDRRA guidelines for funding. The 2011 NDRRA guidelines have an extensive framework of transparency and accountability that was lacking in the 2007 guidelines.⁸

1.17 In the absence of reinsurance, it appears that the Queensland Government Insurance Fund (QGIF) had negligible net reserves to meet any significant new claims such as those that arose during the 2011 disasters. This is after allowing for QGIF's current fund reserves, which essentially only covered its current outstanding liabilities prior to the 2011 disasters. Even if the Queensland government was relying on 75 per cent assistance from the NDRRA, the remaining \$2 billion it requires to self fund cannot be sourced from its own self-insurance fund given that it has negligible reserves.

1.18 Again, the question must be asked: Why is Queensland the only major state government without reinsurance as its own self insurance fund is clearly underfunded and unable to pay any major disaster claims from its own reserves.

Current inquiries and future arrangements

1.19 The majority report noted that the current Natural Disasters Insurance Review, headed by Mr John Trowbridge. This is an important review into matters including, but not restricted to, the NDRRA. In terms of the NDRRA, the Review's Issues Paper noted that:

...the existence of a self-insured fund or captive insurer into which premiums are paid each year represents a level of pre-funding for claims or losses, including losses from natural disasters. Reinsurance taken out by those funds is similarly a form of pre-funding. On this basis, NDRRA recoveries calculated net of reinsurance recoveries can be thought of as a penalty on those States that choose to take out insurance for large losses.⁹

The Review is correct to question whether there are benefits to the States in equity and effectiveness if the NDRRA funding formula were to apply to expenditure gross of reinsurance recoveries rather than net of reinsurance recoveries.

8 The 2007 NDRRA Determination can be found here:
[http://www.ag.gov.au/www/emaweb/rwpattach.nsf/VAP/\(084A3429FD57AC0744737F8EA134BACB\)~NDRRA+Determination+2007.pdf/\\$file/NDRRA+Determination+2007.pdf](http://www.ag.gov.au/www/emaweb/rwpattach.nsf/VAP/(084A3429FD57AC0744737F8EA134BACB)~NDRRA+Determination+2007.pdf/$file/NDRRA+Determination+2007.pdf) The 2011 NDRRA Determination can be found at:
[http://www.ema.gov.au/www/emaweb/rwpattach.nsf/VAP/\(689F2CCBD6DC263C912FB74B15BE8285\)~NDRRA++Determination+2011++Version+1+\(PDF\)+Web+update.pdf/\\$file/NDRRA++Determination+2011++Version+1+\(PDF\)+Web+update.pdf](http://www.ema.gov.au/www/emaweb/rwpattach.nsf/VAP/(689F2CCBD6DC263C912FB74B15BE8285)~NDRRA++Determination+2011++Version+1+(PDF)+Web+update.pdf/$file/NDRRA++Determination+2011++Version+1+(PDF)+Web+update.pdf)

9 Natural Disasters Insurance Review, *Issues Paper*, June 2011, p. 65.

1.20 Further, as the majority report notes, there does need to be some definition of the term 'cost-effective' in the context of the states' insurance policies and NDRRA payments. I agree with the majority report that a common understanding of the term 'cost effective' should be based on an assessment of a state's risk exposure, the geographic spread of its assets, the level of insurance cover it seeks, the excess payable and the premium offered.

The current approach to the market

1.21 Queensland's current approach to the international insurance market must seek a quote to reinsure the state's road network. The Queensland Government's claim that in 2004 it could not secure a reinsurance policy for its extensive road network is questionable. Reinsurance for road infrastructure is available on the international market and should be seriously considered by the Queensland government.

1.22 Moreover, it is important that the Queensland government's quote is properly scrutinised by the Commonwealth government. Australian taxpayers will significantly subsidise the rebuilding of Queensland's public infrastructure through the NDRRA. The quantum of this subsidy can be attributed not only to the scale of the natural disaster but to the state government's failure to reinsure its assets. On this basis, it is critical to protect the integrity of the NDRRA that the states and territories adopt standardised and transparent reporting of their insurance arrangements.

Senator Nick Xenophon
Senator for South Australia

