The Treasury

Residential Flood Insurance Issues Information Release

December 2022

This document has been proactively released by the Treasury/Minister of Finance (Hon Grant Robertson)/ Minister Responsible for the Earthquake Commission (Hon Dr David Clark) on the Treasury website at

https://www.treasury.govt.nz/news-and-events/reviews-consultation/residential-flood-insurance-issues

Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

[25] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information, or who is the subject of the information

[26] 9(2)(ba)(i) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely to prejudice the supply of similar information, or information from the same source, and it is in the public interest that such information should continue to be supplied

[33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by Ministers and officials

[34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions

[35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment

[36] 9(2)(h) - to maintain legal professional privilege

[39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [25] appearing where information has been withheld in a release document refers to section 9(2)(b)(ii).

Accessibility

The Treasury can provide an alternate HTML version of this material if requested. Please cite this document’s title or PDF file name when you email a request to information@treasury.govt.nz.

TE TAI ŌHANGA
THE TREASURY

Reference: T2021/3082 SH-11-4-3-14-2

Date: 15 December 2021

To: Minister Responsible for the Earthquake Commission (Hon Dr David Clark)

Deadline: None
(if any)

Update – Australian reinsurance pool for cyclones and related flood damage

Purpose

This aide memoire updates you on the proposed reinsurance pool in Australia for cyclone and related flood damage. New details about the reinsurance pool have recently been published by the Australian Government with the release of draft legislation for consultation earlier this month.

The reinsurance pool is a useful example to inform options for supporting the availability and affordability of flood insurance in New Zealand. We briefed you on options for progressing the work on flood insurance on 2 December 2021 [T2021/2921].

Key points about the reinsurance pool

The Australian Government has proposed a Government-operated and guaranteed reinsurer to cover all insured cyclone risk for residential home and contents policies and some small business property policies. The reinsurance pool would be funded by premiums charged to insurers.

The purpose of the reinsurance pool is to improve the accessibility and affordability of insurance for eligible properties with high cyclone-risk.

The pool is intended to lower cyclone reinsurance costs overall because it would not charge a profit margin that private reinsurers charge. The benefit of lower cyclone reinsurance costs are intended to be applied primarily to properties with medium-to-high cyclone-risk. Reinsurance premiums on lower cyclone-risk properties are intended to be comparable to private reinsurance premiums. The reinsurance pool is also intended to encourage more insurers to offer insurance in cyclone-prone areas (e.g. Northern Australian), increasing competition and placing downward pressure on insurance premiums.

The Insurance Council of Australia supports the proposed reinsurance pool.

Further detail on the reinsurance pool is set out in Annex 1. We intend to discuss the details of the pool with the Australian Treasury early in the New Year, including clarifying the size of potential premium reductions for higher cyclone-risk properties, whether the policy intent is to cross-subsidise reinsurance premiums between higher and lower cyclone-risk properties, and any advice on developing insurance interventions to support access and availability of private insurance.

Jessica Burns, Senior Analyst, Financial Markets, s9(2)(k)
Dasha Leonova, Manager, Financial Markets, s9(2)(k)

Annex 1: Key design features of the cyclone reinsurance pool

Perils covered by the pool	• Damage caused by a cyclone event (as declared by the Bureau of Meteorology) including damage caused by flooding, storm surge, wind and rain caused by the cyclone weather system.
Eligible property covered by the pool	• Residential home and contents. • Residential strata title buildings (i.e. multi-unit buildings) (where 80 percent of the floor space is mainly residential). • Commercial property (including contents and business interruption) less than $5 million sum insured.
Insurers	• Once fully implemented, insurers will generally be required to reinsure all eligible cyclone losses with the pool.
Funding and premiums	• The pool will be funded by charging reinsurance premiums to insurers. • Premiums will be set to meet the expected claims and operating expenses for the overall pool over the longer-term. • Premiums to medium-to-high cyclone-risk properties are intended to be lower than the private market rate because the pool will not have a profit margin. • Premiums to lower cyclone-risk properties are expected to be comparable to the private market.
Fiscal support	• $10 billion Government guarantee (annually reinstated). • Any shortfall in reserves will be paid for through the Government guarantee. • The overall pool is intended to be cost-neutral to the Government over the longer term.
Administration	• The Australian Reinsurance Pool Corporation (ARPC) will administer the pool. Currently the ARPC provides reinsurance for commercial property and associated business interruption losses arising from a declared terrorist incident. • The Australian Competition and Consumer Commission will receive $18.4 million over five years to monitor and collect data to ensure that savings are passed through to policyholders.
The transition to greater risk-sharing with private insurers	• From 2025, the pool will begin to operate risk-sharing arrangements with insurers whereby some cyclone risk would be returned to private insurers to manage (as opposed to being fully covered by the reinsurance pool).

	The details of the risk-sharing arrangements will be developed later.
Role in incentivising risk reduction	• Over time the pool will offer discounts for policies that cover properties that have undertaken cyclone and flood risk mitigation. • The reinsurance pool will sit alongside other government interventions to mitigate the risks of natural hazards including $600 million to be invested in a new programme of disaster preparation and mitigation which will support projects such as bushfire and cyclone proofing houses.
Implementation timelines	• Insurers will be able to reinsure with the pool from 1 July 2022. • Larger insurers will be required to have obtained reinsurance for all their eligible cyclone risks by 31 December 2023 with smaller insurers having until 31 December 2024.
Key differences with the UK's Flood Re	• Flood Re is owned and operated by private insurers, while the cyclone reinsurance pool is Government run. • Flood Re insures only the highest risk homes, while the cyclone reinsurance pool covers all cyclone risk for all residential buildings and contents insured for cyclone risk (plus some commercial property policies). • Flood Re was intended to be in place for 25 years, while the cyclone reinsurance pool is intended to begin transitioning to risk-sharing with private insurers after three years. • Flood Re supports insurance affordability for higher risk homes through levy-funded cross-subsidies. The cyclone reinsurance pool appears to be more constrained because it supports affordability by passing on savings to higher risk properties from not applying a profit margin.