

## **EXPOSURE DRAFT EXPLANATORY MATERIALS**

### *Terrorism and Cyclone Insurance Act 2003*

#### *Terrorism Insurance Amendment (Cyclone and Related Flood Damage Reinsurance Pool) Regulations 2022*

The *Terrorism Insurance Act 2003* (later renamed the *Terrorism and Cyclone Insurance Act 2003* (the Act)) was established following the terrorist attacks of 11 September 2001 and the withdrawal of terrorism cover by insurance and reinsurance companies. The Act established the Australian Reinsurance Pool Corporation (ARPC) to provide reinsurance cover to insurers for eligible terrorism losses and to perform any other function prescribed in the *Terrorism Insurance Regulations 2003* (renamed the *Terrorism and Cyclone Insurance Regulations 2003* (The TI Regulations)).

The ARPC administers the terrorism reinsurance scheme, which involves providing primary insurers with reinsurance for commercial property and associated business interruption losses arising from a declared terrorist incident.

Section 43 of the Act provides that the Governor-General may make regulations prescribing matters required or permitted by the Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the Act.

On 4 May 2021, the Government announced its intention to establish a reinsurance pool to cover cyclone and related flood damage to commence from 1 July 2022. The cyclone reinsurance scheme seeks to improve insurance access and affordability for households and small businesses in cyclone-prone areas by reinsuring the risk of property damage caused by cyclones and cyclone-related flood damage.

On 15 October 2021, the *Terrorism Insurance Amendment (Cyclones and Related Flood Damage Reinsurance Pool) Regulations 2021* amended the TI Regulations to confer on the ARPC the new function of preparing to operate the cyclone reinsurance scheme.

The purpose of the *Terrorism Insurance Amendment (Cyclone and Related Flood Damage Reinsurance Pool) Regulations 2022* (the Regulations) is to amend the TI Regulations to further refine the framework for the ARPC to operate the cyclone reinsurance scheme. In conjunction with Schedule C to the Treasury Laws Amendment (Measures for a later sitting) Bill 2021: Cyclone reinsurance (the Bill), the Regulations give effect to the announcement in the 2021-22 Budget.

The refinements include:

- Changing the title of the TI Regulations to refer to both the terrorism reinsurance scheme and the cyclone reinsurance scheme;
- Prescribing terms that are referred to in the Bill;
- Setting the threshold amount for determining if an insurer has minimum exposure to policies with eligible risks, and thus whether it is required to participate in the cyclone reinsurance scheme as referred to in the Bill;
- Setting the threshold amount for the maximum sum insured test that applies in determining if certain policies are eligible for coverage under the cyclone reinsurance scheme as referred to in the Bill;
- Providing the information that is required to be contained in the annual Financial Outlook Report as referred to in the Bill; and
- Removing redundant provisions that are no longer relevant.

The Act does not specify any conditions that need to be met before the power to make the Regulations is exercised.

Details of the Regulations are set out in [Attachment A](#).

The Regulations are a legislative instrument for the purposes of the *Legislation Act 2003*.

The Regulations commence the day after they are registered

**Details of the *Terrorism Insurance Amendment (Cyclone and Related Flood Damage Reinsurance Pool) Regulations 2022***

**Section 1 – Name of the Regulations**

This section provides that the name of the Regulations is the *Terrorism Insurance Amendment (Cyclone and Related Flood Damage Reinsurance Pool) Regulations 2022* (the Regulations).

**Section 2 – Commencement**

This section provides that the Regulations commence the day after the instrument is registered on the Federal Register of Legislation;

**Section 3 – Authority**

The Regulations are made under the *Terrorism and Cyclone Insurance Act 2003* (the Act).

**Section 4 – Schedule**

This section provides that each instrument that is specified in the Schedules to this instrument will be amended or repealed as set out in the applicable items in the Schedules, and any other item in the Schedules to this instrument has effect according to its terms.

**Schedule 1 – Amendments**

**Item 1**

**Disallowance**

Item 1 repeals and replaces item 31 of the table in section 10 of the *Legislation (Exemptions and Other Matters) Regulation 2015* to update the name of the Act and ensure that a section 6 declaration continues to be exempt from disallowance.

**Item 2**

**Sunsetting**

Item 2 repeals and replaces item 63 of the table in section 12 of the *Legislation (Exemptions and Other Matters) Regulation 2015* to update the name of the Act and ensure that a section 6 declaration and regulations made under the Act continue to be exempt from sunseting.

**Items 3 to 6**

**Name of Act and Regulations**

Item 3 repeals and replaces regulation 1 to rename the *Terrorism Insurance Regulations 2003* as the *Terrorism and Cyclone Insurance Regulations 2003* (the TI Regulations), consistent with its application to cyclone insurance.

Item 4 updates the short title of the Act to the *Terrorism and Cyclone Insurance Act 2003*.

## **Definitions**

Item 5 updates the definition of **business** to refer to the *Competition and Consumer Act 2010*.

Item 6 provides that the definitions of **cyclone**, **end** (of a **cyclone**) and **reintensify** (in relation to a cyclone) are given by new regulation 3A.

### Item 7

#### **Cyclone definitions**

Item 7 inserts the definition of a **cyclone** for the purposes of section 3 of the Act. If the Bureau of Meteorology (the BoM) observes a weather event that fits the description of a cyclone, BoM will inform the ARPC. Within 24 hours of being notified by BoM, the ARPC will declare the beginning of a cyclone event effective from the time at which the cyclone is recognised by BoM. Any eligible hazard damage arising from a cyclone that satisfies the definition of eligible cyclone loss as defined in section 8C of the Act will be covered by the reinsurance pool from the start of the claims period.

This definition of cyclone is derived from an existing definition used by BoM and is based on the current scientific assessment of what constitutes a cyclone.

Item 7 inserts the definition of the **end** of a cyclone. After first observing that a cyclone has occurred (and triggering the declaration mechanism covered above), when the BoM observes a weather event no longer meets the criteria of a cyclone, according to the description of an end of a cyclone, BoM will inform the ARPC. Within 24 hours of being notified by BoM, the ARPC will declare the end of a cyclone event. The claims period will last for a fixed additional period after the time at which the end of a cyclone is recognised by BoM. Any eligible hazard damage arising from a cyclone that satisfies the definition of eligible cyclone loss as defined in section 8C of the Act will be covered by the reinsurance pool until the end of the claims period.

This definition is based on the current scientific assessment of what constitutes the end of a cyclone.

Item 7 also defines when a cyclone would **reintensify**. After a cyclone is downgraded, it is taken to reintensify if it again meets the condition in paragraph (2)(b) of regulation 3A. In this case, on the advice of BoM, ARPC would declare a new cyclone event.

## Item 8

### **Threshold for mandatory participation**

Item 8 prescribes \$10 million as the threshold for gross written premiums payable for the previous financial year (for policies with eligible cyclone risks) for the purposes of determining mandatory participation under section 8A of the Act. Subject to the application provisions, if an insurer exceeds this threshold, they are required to participate in the cyclone reinsurance scheme for the next calendar year and therefore must reinsure all eligible cyclone losses with the ARPC. If an insurer is below this threshold, participation in the scheme is voluntary for it.

### **Maximum sum insured for non-residential policies**

Item 8 prescribes \$5 million per policy as the maximum sum insured threshold for non-residential policies for the purposes of section 8B(3)(d) of the Act. This threshold is inclusive of the total of the property sum insured, contents sum insured and business interruption sum insured. The threshold applies to buildings, contents or both that are not used principally and primarily as a place of residence.

If an insurer has a single or a combined non-residential building, contents or business interruption insurance policy sum insured of more than \$5 million, then the risk under that policy cannot be reinsured by the insurer with the ARPC under the cyclone reinsurance scheme.

### **Hazard coverage definitions**

Item 8 defines *storm surge* for the purposes of section 8C(b)(ii) of the Act and is derived from an existing definition used by BoM. Losses that arise from storm surges caused by a cyclone (for the duration of the claims period) will be an eligible cyclone loss and therefore covered by the scheme.

Item 8 defines *flood* for the purposes of section 8C(b)(iii) of the Act as a flood defined by subsection 34(1) of the *Insurance Contract Regulations 2017*. Losses that arise from flooding caused by a cyclone (for the duration of the claims period) will be an eligible cyclone loss and therefore covered by the scheme.

### **End of claims period in second declaration**

Item 8 prescribes that, for the purposes of section 8F(3), the duration of time between the end of a cyclone and the time at which the claims period ceases is 48 hours. This will be specified in the declaration made by the ARPC under section 8E(2).

### **Reporting**

Item 8 provides that, for the purposes of the Financial Outlook Report (section 40A(1) of the Act), the ARPC must report on the matters prescribed. The ARPC is required to provide yearly reports on the operation of the cyclone scheme to ensure it operates in a transparent and publicly accountable manner.

## Item 9

### **New functions for ARPC**

Regulation 6 prescribes additional ARPC functions. Item 9 repeals regulation 6 as these functions are no longer necessary nor required. When the Act commences it establishes the new function under which the ARPC operates the scheme, resulting in the regulation being redundant. Furthermore, the National Insurance Affordability functions are no longer in operation.

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