

EXPLANATORY STATEMENT

Issued by the Authority of the Assistant Treasurer

Terrorism Insurance Act 2003

*Assistant Treasurer to Australian Reinsurance Pool Corporation (Premiums)
Directions 2011*

Subparagraph 38(2)(d) of the *Terrorism Insurance Act 2003* (the Act) provides that the Minister may give written directions to the Australian Reinsurance Pool Corporation (ARPC) setting premiums that the ARPC is to charge in respect of contracts of insurance. The Act established the ARPC and the framework for the Government's terrorism insurance scheme. The Act effectively deems terrorism risk cover into eligible insurance contracts by rendering terrorism exclusion clauses void. Insurance companies may then reinsure their additional risk with the ARPC, in which case a premium is payable to the ARPC. The premium payable is calculated according to a system of tiers which are set by reference to postcodes.

Section 41 of the Act requires that a review of the need for the Act to continue in operation must be undertaken at least once every three years after commencement. The most recent review was completed by 30 June 2009 and released by the Treasurer in October 2009. The Government agreed to all of the review's recommendations.

One of the recommendations was that the Treasury, with the assistance of an outside contractor, update the allocation of individual postcodes to particular tiers to ensure that all postcodes are allocated to the correct tier. This process has been completed. The *Assistant Treasurer to Australian Reinsurance Pool Corporation (Premiums) Directions 2011* ("2011 Directions") formalises the updated allocation of postcodes.

All Australian postcodes are allocated to one of three 'tiers' which are broadly representative of risk. Postcodes allocated to tier A are those covering the CBD areas of Australian cities with a population of over one million. Postcodes allocated to tier B are those covering the urban areas of all State capital cities and cities with a population of over 100,000. Postcodes allocated to tier C are those postcodes not allocated to either tier A or B.

Reinsurance premiums are set at 12 per cent, 4 per cent and 2 per cent of the insurer's underlying premium income, for insured properties in postcodes in tiers A, B and C respectively. These rates have remained unchanged since they were first set by the *Treasurer to Australian Reinsurance Pool Corporation (Premiums) Direction 2003* ("2003 Direction"). The 2003 Direction also created the first postcode allocation list to assign each postcode to an appropriate tier. This list has remained largely static since 2003.

The *Treasurer to Australian Reinsurance Pool Corporation (Premiums) Direction 2007* ("2007 Direction") introduced a facility for the ARPC to automatically update the postcode allocation list, but only in limited

circumstances: when existing postcodes are partitioned; when the boundaries of postcodes are changed; or when the boundaries of tier A or B ‘population centres’ change.

The 2009 review of the Act found that demographic changes since 2003 have resulted in some postcodes no longer being allocated to the correct tiers, resulting in inequities in the scheme. For instance, increases in population density may necessitate some postcodes being re-assigned to higher tiers. These changes cannot be captured by the automatic update facility introduced in the 2007 Direction.

The 2011 Directions updates the postcode allocation list to ensure that all postcodes are allocated to the correct tiers, in accordance with the methodologies described above, so that appropriate premiums may be charged to reinsure properties in those postcodes. The complete, revised postcode allocation list can be found at Schedule 1 of the 2011 Directions. The 2011 Directions also repeals the 2007 Direction.

Apart from changes to the postcode allocation list and changes in the phrasing of certain clauses to improve clarity, the 2011 Directions does not substantially alter to operation of the scheme.

The 2011 Directions is a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

The Treasury consulted with Geoscience Australia in preparing an updated postcode allocation list. Geoscience Australia employed a ‘geoprocessing’ model based on the urban boundary area as defined by the Australian Bureau of Statistics (ABS). The ARPC gave advance notice (in writing) of the proposed changes to the postcode allocation list to all of its clients, and received no adverse feedback from any clients.

The 2011 Directions commence on 1 July 2011.