

# Queensland Floods Commission of Inquiry

## Submission on behalf of Suncorp Group Limited

We refer to Commission's letter dated 7 March 2011, and in particular the indication that leave would not be granted to Suncorp Group Ltd and its subsidiaries (**Suncorp**) to appear in relation to the terms of reference 2(f) and 2(g).

This submission is written in response to the Commission's invitation in the letter dated 7 March 2011 to provide further information in support of Suncorp's application for leave to appear in relation to the terms of reference 2(f) and 2(g).

We note also that the Commission has invited written submissions 'relating to issues of flood preparedness relevant to next summer's wet season (particularly dam operations, early warning systems and responses)', and that those submissions are required to be received by the Commission by 5.00pm, 11 March 2011. The matters addressed below also address these issues, and we ask that the Commission treat this submission as also being a submission on behalf of Suncorp for that purpose.

### **1. Background**

- 1.1. The management of natural hazard risk is a collective responsibility of governments, insurers, businesses, communities and individuals and requires an integrated approach to matters such as water management including dams and levees, land zoning and building design, emergency response and community education about matters such as understanding and protecting properties, local emergency alerts and evacuation.
- 1.2. It is in the interests of individuals, business, insurers and government for there to be a healthy and competitive insurance industry able to offer appropriately priced and affordable insurance to cover natural hazard risks. The key to success in providing comprehensive cover for natural hazards is the ability to accurately assess and price risk. Comprehensiveness of cover falls, and price increases, directly in relationship to the level of uncertainty in the ability to quantify risk.
- 1.3. Management of water infrastructure is a key component of being able to quantify risk, and therefore of the ability to offer, the price of, and the scope of cover in, insurance policies covering flood risk.
- 1.4. The recent floods that particularly affected south east Queensland have called into question many of the underlying beliefs and assumptions regarding flood risks in Queensland. An understanding of this, and certainty in relation to future management of water infrastructure is more critical than ever in understanding risk from an insurance perspective. As the major provider of flood insurance in Queensland, Suncorp believes that it should have the opportunity to contribute to the Inquiry on the issue of dam operations, future management of water infrastructure, and the other matters raised in paragraph 1.1.

### **2. Regulation of insurers**

- 2.1. The insurance market in Australia is highly regulated. By way of brief outline:

- 2.1.1. Only general insurers and reinsurers authorised by Australian Prudential Regulation Authority (APRA), can offer general insurance and reinsurance in Australia.
- 2.1.2. For the protection of policyholder interests, APRA will only authorise insurance companies which have the capacity and commitment to conduct insurance business on a continuing basis, with integrity, prudence and professional skill.
- 2.1.3. Insurers are required to have in place a reinsurance management framework in accordance with Prudential Standard GPS 230 Reinsurance Management. The framework must include a reinsurance management strategy (REMS) that describes the key elements of the reinsurance management framework, supporting policies and procedures and clearly defined managerial responsibilities and controls. GPS 230 sets out the approach APRA will use to assess the adequacy and appropriateness of an applicant's policies and procedures proposed for identifying, managing and monitoring reinsurance arrangements. (GPS 230 can be downloaded from the APRA website.)
- 2.1.4. An insurer's capital base must be greater than its minimum capital requirement (MCR). For insurers incorporated in Australia (including foreign-owned subsidiaries), the capital base is generally equivalent to the net assets of the insurer, together with any excess technical provisions above the minimum 75% probability of sufficiency level of net insurance liabilities and any other eligible capital instruments, adjusted for any deductions specified by APRA.
- 2.1.5. It is critical for insurers to be able to calculate with a reasonable degree of accuracy the net insurance liabilities and the probability of the liability arising in order to appropriately price the risk and also manage the risk in accordance with the prudential standards including reinsurance management.
- 2.1.6. Insurers are required to provide APRA with an outline of reinsurance arrangements, per risk and per event retentions, and evidence that reinsurers are willing to provide the reinsurance cover.

### **3. Ability to offer insurance**

- 3.1. In order to offer insurance to customers, and to acquire reinsurance, it is therefore necessary for both general insurers and reinsurers to be able to:-
  - assess the likely frequency and severity of particular risk events based on historical data and estimations of future event occurrence patterns;
  - understand the effect of risk mitigation strategies (such as flood mitigation capacity of man made structures including flood levees and dams);
  - understand and have a level of confidence in the robustness of the processes by which government infrastructure including power, water, sewage, and other amenities are managed;
  - assess the level to which risks are (or are not) ameliorated by local planning laws and other regulatory requirements for buildings and other insurable interests;
  - appropriately price the risk; and

- have prudentially sound reinsurers willing and able to accept a transfer of part of the risk at an appropriate cost, in accordance with Prudential Regulation and approved REMS.
- 3.2. To price the risk, it is necessary that general insurers and reinsurers have access to information which enables them to:
- accurately define the insurable event;
  - calculate the probability of the insurable event occurring;
  - calculate the potential liability for compensation if the insurable event occurs; and
  - assess the extent to which risk can be discounted due to any mitigating factors eg dam management.
- 3.3. In the context of flood insurance, this includes accessing:
- local authority flood maps;
  - reports on the construction, flood mitigation effect and management strategies for water infrastructure such as Wivenhoe Dam; and
  - historical data on weather and flooding dating back to the 1800s.
- 3.4. The quality of the information available to insurers directly influences the extent to which the information can be relied upon in pricing risk. Ideally, insurers and reinsurers seek to access information which is adequate, transparent and independently verifiable. In relation to matters over which insurers have no direct control, such as dam management strategies, it is essential that:
- the information made available to insurers is accurate and meaningful;
  - the underlying policies, procedures and strategies are sound; and
  - there are mechanisms in place to ensure compliance with the underlying policies, procedures and strategies, so far as is reasonably possible.

#### **4. Insurance and re-insurance arrangements specific to Suncorp**

- 4.1. Suncorp companies offer cover for loss or damage to homes caused by storm and flood (excluding AAMI in the case of riverine flood). Suncorp is one of the only major insurers operating in the domestic insurance market that offers cover as standard.
- 4.2. Suncorp insures approximately 37% of Queensland households. Companies within the Suncorp Group insure approximately 17% of Queensland businesses.
- 4.3. Suncorp's potential claims cost arising out of the January flood event is in the order of \$800-\$900 million. Additionally it also suffered significant flood damage to its own buildings in South East Queensland including two call centres and nine branches, as well as losing access to Brisbane CBD commercial premises.
- 4.4. Suncorp has offered flood cover as standard on its Suncorp and GIO brands since 2007. It has been able to offer that cover, where other insurers do not offer flood cover at all or offer it only as an option subject to acceptance criteria and/or with limits on cover, for a number of reasons, including that:
- 4.4.1. Suncorp has expended substantial amounts in developing a specific information base, including extensive hydrological information addressing flood mapping, on a property by property basis. The information base has

been developed by Suncorp using both internal teams and external consultants. It has a substantial investment in the data base, which it treats as its confidential intellectual property.

- 4.4.2. The information is used by Suncorp not only for the purposes of pricing insurance premiums on a property by property basis, but also in its annual negotiations with re-insurers.
- 4.4.3. The negotiations undertaken by Suncorp on an annual basis with re-insurers also proceed upon the basis of a number of underlying assumptions, including assumptions as to dam levels in Wivenhoe Dam and Somerset Dam, the effectiveness of those dams for the purposes of flood mitigation, as well as predictive weather information and information derived from Suncorp's information data base relating to properties and the assessment relevant flood risks; and
- 4.4.4. Pricing of premiums in South East Queensland occurs on a property specific basis utilising mapping from Suncorp's information data base. Matters relevant to pricing include building levels and heights, construction methods and planning policies.
- 4.5. Changes in dam operations, flood mitigation policies and planning policies will directly impact upon the accuracy and reliability of the information contained in Suncorp's information data base, and could potentially impact Suncorp's ability to accurately assess flood risk, price it appropriately and obtain reinsurance cover.
- 4.6. Last financial year, Suncorp acquired reinsurance cover up to \$5.6 billion at a cost of approximately \$580 million.
- 4.7. As will be appreciated, in the events that have occurred, it is expected that negotiations with re-insurers in respect of Queensland risks going forward will be much more difficult and demanding. It is expected that re-insurers will require a much more detailed level of information than has been the case in previous negotiations.
- 4.8. In particular, it is anticipated that previously held assumptions as to the effectiveness of Wivenhoe Dam as a flood mitigation measure will no longer apply. The findings and recommendations of the Inquiry will directly affect the extent to which Wivenhoe Dam can be seen as a basis for discounting the risk of flood for a substantial number of properties and businesses. They will therefore directly affect the ability of Suncorp to offer flood cover in Queensland in its present form, the cost at which it may be able to do so, and its ability to source reinsurance at a commercially acceptable price.
- 4.9. That Suncorp has a direct and significant interest in wet season events in Queensland is demonstrated by the fact that Suncorp received a high level briefing by the Bureau of Meteorology in October 2010 about the likely severity of the forthcoming wet season including likely cyclone activity.
- 4.10. As will be appreciated from what has been outlined above, Suncorp is acutely interested in:
  - 4.10.1. Ongoing dam management and the basis of any recommendations for balancing the need for water storage with flood mitigation: In particular in relation to Wivenhoe Dam, flood mitigation is an equally important function to that of water storage. Indeed, it is arguably a more critical purpose of Wivenhoe Dam given the additional alternative water supply

infrastructure which has been constructed or consolidated since the construction of Wivenhoe Dam for the purposes of water storage and guarantee of water supply. In order to mitigate the risks of a repeat of the devastating impacts of the January 2011 floods, the Commission should consider whether it is appropriate to maintain the Wivenhoe Dam at a lower capacity (by earlier and more frequent releases) and on what information such decisions should be made eg long range weather forecasts, La Nina weather patterns, the formation of cyclones etc.

- 4.10.2. The level of flexibility which should be afforded to water management authorities in managing dam levels: Since the January floods, SEQ Water has implemented water releases, reportedly to reduce the Wivenhoe Dam water storage to 75% of capacity. In order to be able to model and appropriately price flood risk post the recent event, insurers will need to understand the extent to which operators will have discretion as to management of Wivenhoe Dam in the future.
- 4.10.3. Water release strategies and recommendations which may be made by the Commission concerning the basis upon which water releases may occur in the future.
- 4.10.4. A critical review of dam management procedures and decisions which occurred in relation to the 2011 event: Understanding why these decisions were made will assist in assessing risk for the future.
- 4.10.5. Recommendations for changes to the local authority building requirements in flood prone areas including:
  - (a) the extent to which flood impact assessment should be built into development and infrastructure approval processes;
  - (b) recommendations addressing local authority planning instruments and approvals; and
  - (c) the extent to which development and infrastructure design should be required to take into account the impact of proposed development after a heavy downpour and prolonged rain events, on existing properties as well as new developments.
- 4.10.6. Findings in relation to, and recommendations regarding, government and infrastructure management authorities' response to long range weather forecasting.
- 4.10.7. Flood crisis planning and management recommendations.
- 4.10.8. Early warning systems: government powers to require evacuation of people and movable property.
- 4.10.9. Recommendations as to construction and maintenance of other potential flood mitigation infrastructure eg permanent or temporary levees around population areas and along creeks and rivers prone to flooding.
- 4.10.10. Recommendations addressing management of storm water pipes which empty into the Brisbane River to prevent flooding from pipe overflows eg Suncorp Stadium and Brisbane Corso.
- 4.10.11. Recommendations as to enhancement of the local authority flood mapping information.

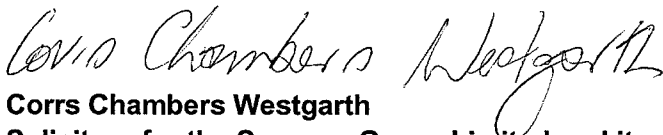
4.11. If it is not possible to get a sufficient level of comfort that there will be appropriate:

- (a) management of dams;
- (b) flood mitigation infrastructure and management; and
- (c) building standards and requirements in flood prone areas,

it may not be possible to economically price insurance, or acquire reinsurance, of flood prone areas of Queensland for the next wet season and future years.

## **5. Suncorp's interests adversely affected**

- 5.1. For the reasons identified above, there exists the prospect of findings and recommendations adverse to Suncorp's interests, including recommendations which if implemented, will inhibit Suncorp's capacity to continue to offer flood insurance in the Qld market.
- 5.2. Suncorp seeks to be afforded an opportunity to put before the Commission informed submissions addressing the impact which adoption of proposals or recommendations made in submissions by other interested parties concerning flood preparedness relevant to next summer's wet season (including dam operations, early warning systems and responses) may have upon its ability to place re-insurance in the immediate short term as well as the long term, its ability to continue to offer flood cover in its current format going forward and the impact of those proposals on future premiums levels.
- 5.3. The making of informed submissions to the Commission necessarily requires, in the first instance, that Suncorp be appraised of the submissions made by other interested parties, and that it subsequently be permitted to participate in any hearings in which they will be addressed and evaluated.



**Corrs Chambers Westgarth**  
**Solicitors for the Suncorp Group Limited and its subsidiaries**