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Update from the Flood Working Party

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Contents

- The issue – affordability and availability of flood insurance threatened by better pricing
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- What should the actuarial profession be saying?

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GIRO Flood Working Party

Aim: To be a source of knowledge and expertise within the Actuarial Profession on matters relating to flood with a particular focus on the UK.

- To develop the Profession's position on UK flooding.
- To produce reference material for UK actuaries.
- To improve the understanding of flood risk amongst the industry, government and public.
- **To gather data and opinions from the industry to inform the above.**
- To work with industry bodies to report on market developments following the expected launch of Flood Re in 2015.

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The issue

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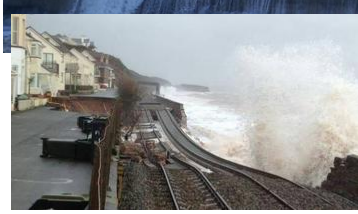
Flooding - an issue in the UK



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22 April 2015 Source: Met Office 6

Flooding – a brief UK history

- 2004 Boscastle
- 2007 UK Floods: Widespread flooding in June and July
- 2009 Cumbrian Floods
- 2012 UK Floods: Wettest April in 100 years
- 2013/14 Winter Floods/Storms: Widespread persistent flooding

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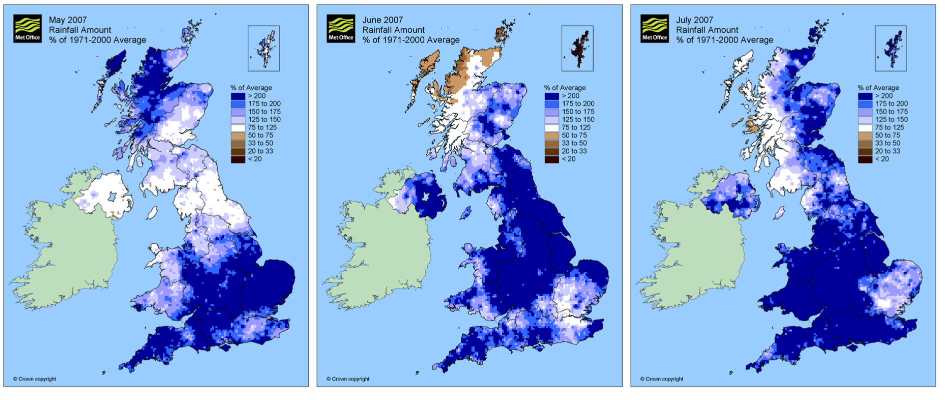
Source: Wikipedia

2007 floods



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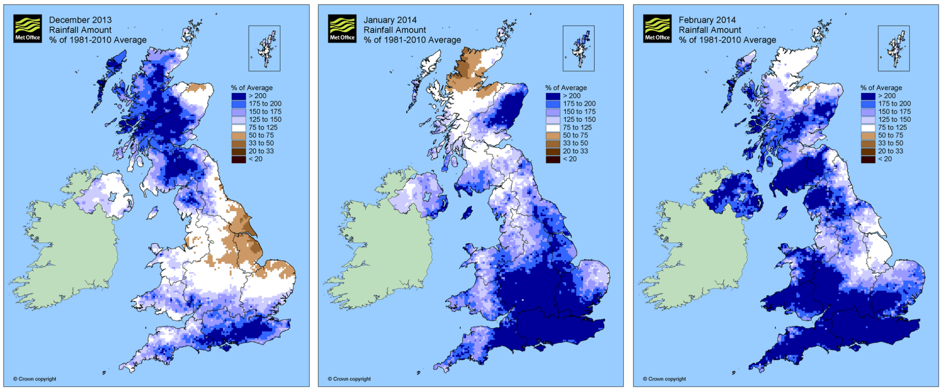
Source: Met Office

2013-2014 Winter floods



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Insurance cost – 2013/2014

18,700 Flood claims

£451m Flood claims cost

448,300 Storm claims

£640m Storm claims cost

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Trends in weather patterns

- 2014 was the UK's warmest ever year and eight of the top ten warmest years have occurred since 2002.
- Five of the UK's top six wettest years have occurred since 2000.
- Many models are based on the average of past years. However, there is some evidence that expectations for 2015 should be greater than the average of past years.

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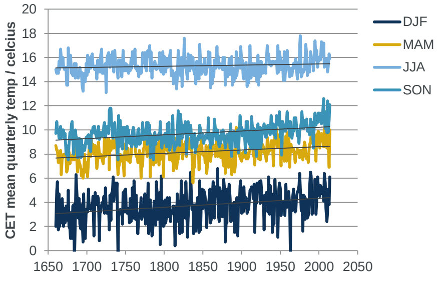
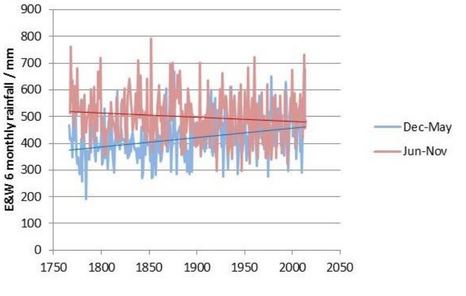
Trends in weather patterns



Trend for a warmer time than recorded in the past – this increase in energy is expected to lead to more storms and greater rainfall as warmer air can carry more moisture.



The impact on rainfall is less clear – winters have been wetter and summers drier over the last 250 years but more recently summers also appear to be wetter again.

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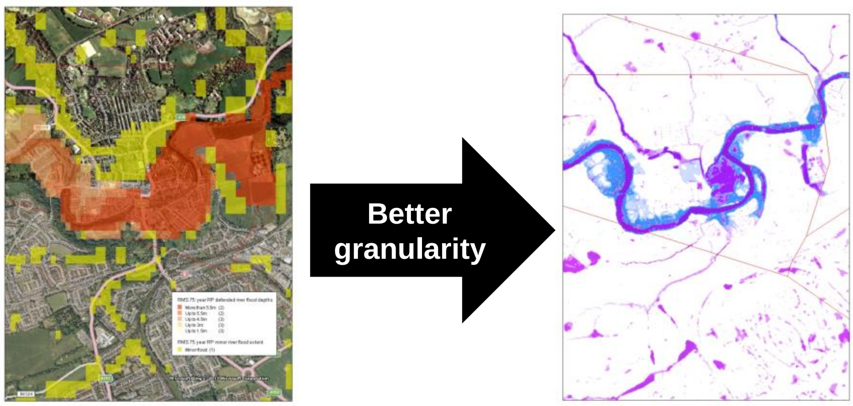
Insurers

- Insurers have got much better at predicting flood risk at a more granular level. This has seen the expected flood cost for the worst properties become more extreme leading to a problem of affordability and availability.



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Flood Re

What is Flood Re?

- Designed to enable high flood risk households to obtain affordably priced flood insurance, Flood Re is an agreement between UK insurers and the Government to allow insurers to pass the flood risk element of a home insurance policy into a not-for-profit fund that will pay any subsequent flood claim.
- Aim is to allow a sustainable transition to risk reflective pricing over 25 years.

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Property coverage

- Flood Re is designed to provide support to those homeowners who, without it, are most likely to face problems in obtaining affordable flood insurance.
- Exclusions include:
  - Homes built after 1 January 2009
  - Commercial properties, including commercial leasehold properties (although there are some exceptions)

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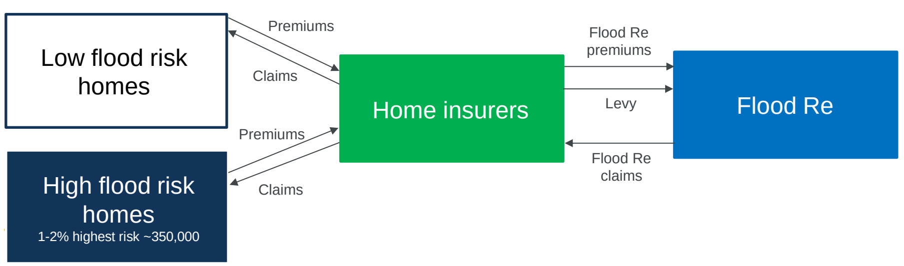
Why is Flood Re necessary?

- In face of the rising flood risk, the ABI has estimated that between 300,000 – 500,000 flood-risk UK households would struggle to obtain affordably priced flood insurance without a scheme like Flood Re.
- The Government and others agreed with the ABI that the Flood Insurance Statement of Principles established in 2000 had become unsustainable.

How will Flood Re work?



How will Flood Re work?

- Insurers can reinsure domestic property insurance flood risks for homes built prior to 2009 with a not for profit pool for a fixed cost depending on council tax band and cover type:

Cover Type		Property Council Tax Band							
		A	B	C	D	E	F	G	H
	Wales:	A/B/C		D	E	F	G	H	I
Buildings only		£132	£132	£148	£168	£199	£260	£334	£800
Contents only		£78	£78	£98	£108	£131	£148	£206	£400
Buildings and Contents combined		£210	£210	£246	£276	£330	£408	£540	£1,200

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Who pays?

- The insurance industry is paying the £10m set up costs to get Flood Re up and running. The Flood Re pool itself has two sources of income:
  - Premiums of flood risks passed by insurers, which will be capped based on Council Tax bands.
  - An additional levy on the industry, equivalent to the existing cross-subsidy that exists in the market. This will be around 2.2% of a policy which equates to a notional average of £10.50 per customer.

Possibility of a further levy (Levy II) if Flood Re cannot meet its funding requirements.

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Flood Re funding

- Flood Re will purchase its own reinsurance and hold reserves and capital so that it can fully cover all claims in at least 99.5% of years.
- While Flood Re is being developed, ABI members are voluntarily continuing to meet their commitments to existing customers under the old Flood Insurance Statement of Principles agreement.
- The Government has committed to a specified level of flood defence spending for 2015/16. They will also ensure adherence to planning guidelines to avoid developments in areas at high risk of flooding.

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Strengths and issues

Strengths

✓ Provides coverage for consumers – a market for new business

✓ Very likely to improve price/terms for majority of customers who are subject to high flood risk

✓ Properties built since 2009 cannot be ceded to Flood Re – this introduces a pressure on planning to fully consider flood risk

✓ Intention to return to risk reflective premiums within 25 years encourages investment in defences and improvement of housing stock (by owners)

✓ Some scope for resilient repairs

✓ Provides a focus for the flood debate

Issues

✗ There is little in Flood Re to encourage the Government to invest in flood defences

✗ Flood Re will only cover the costs from an event up to the expected 1 in 200 level

✗ Does not cover all properties

✗ Existing cross subsidies remain

✗ Uncertainty around Levy II

✗ Deemed to be expensive

✗ Operationally difficult for insurers to cede all properties they may want to

Issues

- ✘ Requirement for insurers to set up new processes
- ✘ Insurers will cede poor risks
- ✘ Perceived to benefit the wealthy as well as the poor?
- ✘ Concerns at who pays and the impact this could have on general insurance take-up
- ✘ Skews market in favour of insurers who have previously written more cross-subsidised flood risk
- ✘ The 25 year return to risk reflective pricing is subject to political uncertainty

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Progress

- A number of delays see the Flood Re programme slightly behind plan for end November 2015 launch.
- Waiting on PRA authorisation.
- Delays in technical specs for insurers and perhaps slow engagement from some quarters means time to insurer readiness is uncertain and may not fit in with planned 2015 live date.
- Flood Re's intention is not to launch until there is sufficient market readiness – to not give an advantage to insurers involved early on, even if this sees launch slip to end Q1 2016 say.

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Thoughts on who should pay for flood insurance/ repair?

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What should the actuarial profession be saying?

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Conclusion

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Conclusion

- It seems likely Flood Re will achieve the core aims of improved affordability and availability of insurance.
- There are a number of disincentives to write additional flood business but political pressure seems likely to deliver a more competitive market in flood risks.
- Insurers who have much subsidised flood risk on their books may just see this as a formalisation of their current approach. For insurers who don't, it produces a relative competitive disadvantage.

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Expressions of individual views by members of the Institute and Faculty of Actuaries and its staff are encouraged.

The views expressed in this presentation are those of the presenters.

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