HOUSE OF COMMONS LIBRARY

BRIEFING PAPER

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Household flood insurance

By Timothy Edmonds

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Summary

The continued general availability of domestic flood insurance (the commercial market is excluded from this scheme) at reasonable cost had been under pressure for some years following an increase in the number and severity of flood events.

The increased incidence of localised flooding present insurers with a dilemma. They could either:

- carry on as before, and face repeated, huge, claims from a minority of claimants, which is unprofitable for them,- or
- due to better statistical and environmental data, restrict the availability of insurance offered to exclude areas prone to flooding or introduce substantially differentiated premiums for people in different areas.

Commercial considerations weighed heavily on that choice and the availability of insurance in flood risk areas (at any price) became noticeably restricted as insurers pulled out of the market.

Mindful of the social consequences of a market failure, government sought, with the industry, a long-term solution which encompasses a reduction in the totality of risks (better flood defences) whilst maintaining, to a degree, of the traditional 'pooling of risks' pricing model and the minimum of market interference.

Formal moves to find a solution began with a Flood Summit in September 2010 which discussed what would happen to flood insurance after 2013. Three working groups were set up to take forward a work programme. The groups were comprised of representatives from government, the Environment Agency, the insurance industry and related organisations. The period up to 2013 was characterised by efforts on behalf of both the industry and government to find a long term solution. These efforts were against the backdrop of a temporary industry - government agreement expiring in the summer of 2013.

What emerged was a 'pact', in 2015, between both sides which would be governed by agreed statement of principles and a new insurance vehicle – Flood Re. The main points of the 'pact' are

- a commitment by the industry to offer insurance in high risk areas at affordable prices;
- the establishment of the Flood Re scheme run by the industry;
- a guarantee that the government would be primarily responsible for losses due to 'a catastrophic event' that Flood Re could not meet; and
- increased government spending on flood defences.

The primary legislative framework for Flood Re is the *Water Act 2014*, which received Royal Assent on 14 May 2014. The 2014 Act commenced with effect from 1 January 2015. The Flood Re Regulations put in place the secondary legal framework including its funding and administration. Flood Re went live in April 2016.

A Library Research Paper includes details of the Bill.

Flood Re has its own website now. Many questions that Members or constituents might have are covered simply on its FAQ pages.

This note discusses the background to this issue, explains the final agreed solution and describes what householders can do to keep their flood-related insurance premiums

down. Information about insurance aspects of this topic should be addressed to Timothy Edmonds (x4318), questions about flood defence measures to Sarah Priestly (x2930).

1. Introduction

Household flood risk in the UK has historically been covered by standard household insurance—in many other countries the government is the insurer of last resort for flooding, or flood insurance is bought separately from normal household insurance.[1]

Currently, insurance premiums often do not fully reflect the actual flood risk to properties. As a result "the costs of flood damage are often shared between the premiums of all householders, whether or not they are at risk of flooding". This cross-subsidy means that "many householders living in high-risk properties may not be paying a price which reflects the risk".[2]

Insurance is fundamentally a way of reflecting and reducing risk. If all groups face generally the same risk of an event, standardised levels of premiums can be used to pool the risk fairly amongst the population. However, as incidences of localised flooding appear to have become more common insurers have faced a dilemma. They can either:

- carry on as before, and face huge claims from a minority of claimants which make the service unprofitable, or,
- due to better statistical and environmental data, restrict the availability of insurance offered to exclude areas prone to flooding or introduce substantially differentiated premiums for people in different areas.

Since the former option is not sustainable in a commercial way in the long term, left to itself the industry will adopt the second option. But the consequences of this are not attractive socially. Properties with a flood claims experience would face huge increases in premiums if their policies were to be commercially viable, or the industry would simply restrict cover which would create enormous problems for large sections of the property market.

Buildings insurance is not mandatory however, it would be virtually impossible to get a mortgage on any property that was not fully insured. Hence, such properties could only be sold to cash only buyers. From a consumer 'PR' point of view, both outcomes are unattractive to the insurance industry.

The industry has already adapted to a degree. The cross-subsidy is expected to diminish over coming years as insurers more accurately reflect flood insurance risk in premiums. This may lead to lower insurance costs for most people, but large cost increases for those in high flood risk areas.[3]

Some insurers already refuse to insure in certain areas, or will continue to do so only for existing customers. Mindful of the social consequences of a market failure, the government has sought with the

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1 The Pitt Review: Learning lessons from the 2007 floods, Cabinet Office, June 2008
2 Flooding and insurance: a roadmap to 2013 and beyond: An interim report of the flood insurance working groups, Defra, May 2011
3 Flood risk and insurance: A roadmap to 2013 and beyond: Final report of the flood insurance working groups, Defra, December 2011

industry to find a long term solution which encompasses a reduction in the totality of risks (better flood defences) and a continuation to a degree of the traditional pooling of risks pricing model. What emerged was a 'pact' between both sides which would be governed by agreed statement of principles.

2. The original statement of principles

Flood insurance provision was guided by a statement of principles first agreed in 2002 between the then government and the Association of British Insurers (ABI). This was a set of commitments by the industry to provide flood insurance for domestic properties and small businesses "for as many customers as possible". Insurance premiums and other terms—such as excesses—would be based on an assessment of the risk of flooding "but will be offered in a competitive market". It also stated that continued provision of insurance was dependent upon action by the Government to reduce flood risk by investing in defences. Put simply, the industry would provide cover where homes were protected at or above government minimum standards of flood defence and those properties which would be covered in the future by planned improvements to flood defences. An ABI press release outlined the key terms of the agreement:

> The **Statement of Principles** has five objectives
>
> - full access to a competitive market for insurance for the vast majority of homeowners and small businesses;
> - improved security for those who live and work in high-risk areas;
> - new provisions for those who wish to sell their homes or businesses;
> - better use of new solutions to make properties insurable, even in high-risk areas where improvements to flood defences are not planned;
> - a clear incentive for Government and local authorities to continue to invest in flood defences.
>
> Around one in ten of the UK's 20 million homes and businesses is situated in the floodplain. The vast majority of these – around three quarters – are protected against the risk of flooding at or above the Government's own minimum standards, and ABI members will continue to make flood cover available for them as a standard feature of household and small business policies. Premiums and other contract terms will reflect the different levels of flood risk, as they do for other factors such as crime.
>
> The new Statement of Principles will also benefit policyholders who face higher risks of flooding (i.e. are not protected to the Government's minimum standards). Where improvements in flood defences sufficient to meet the Government's standards are scheduled for completion by 2007, insurers will maintain flood cover for homes and small businesses which they already insure. Going beyond the terms of the existing two-year agreement, insurers will also make special efforts to maintain cover for properties when they are sold, subject to satisfactory information about the new owners and proposed use of the premises.

> Where improvements in flood defences are not planned, insurers will "examine the risks on a case by case basis and use their best efforts to continue to provide cover." The Statement of Principles commits insurers to work with policyholders where necessary to see if action can be taken to make the property insurable. This might include the use of accredited flood protection products and temporary defences.[4]

Extreme rainfall in 2007 led to widespread flooding in England and Wales. It was arguably the largest peacetime emergency since World War II, causing 13 deaths and £3.2 billion in damage.[5][6] In response the Labour Government commissioned Sir Michael Pitt to undertake an independent review of the floods. It concluded that "urgent and fundamental" changes were needed to reduce flood risk. However, it generally supported the arrangements for flood insurance provision.

Following a review of flood insurance in 2008 the ABI and government updated the statement of principles. It ensured that cover would continue to be available to the vast majority of householders. The Department for Environment, Food and Rural Affairs (Defra) website summarised the changes:

> The revised statement... ensures that flood cover will be available as a standard feature of household and small business policies for a) those properties defended to a minimum standard of 1 in 75 (in other words where the design standard of defences is such that the probability of the properties being flooded in any single year is 1.3% or less), or b) for those properties where such defences are scheduled for completion within the next five years. Premiums will continue to reflect different degrees of risk.[7]

The statement does not apply to buildings constructed after 1 January 2009.[8]

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4 Statement of Principles, ABI press release November 2002
5 The cost of the 2007 floods, Environment Agency, January 2010
6 The Pitt Review: Learning lessons from the 2007 floods, Cabinet Office, June 2008
7 Defra Website as of 10 December 2009
8 Flooding and insurance: a roadmap to 2013 and beyond: An interim report of the flood insurance working groups, Defra, May 2011

3. The build up to 2013

3.1 The Flood Summit working group

The period up to 2013 was characterised by efforts on behalf of both the industry and government to find a long term solution. A Flood Summit in September 2010 discussed what would happen to flood insurance after 2013.[9] Three working groups were set up to take forward a work programme. The groups were comprised of representatives from government, the Environment Agency, the insurance industry and related organisations.

Working Group 1 considered future flood insurance models, it agreed a set of common principles that a model should address:

> 1. Insurance cover for flooding should be widely available
>
> 2. Flood insurance premiums and excesses should reflect the risk of flood damage to the property insured, taking into account any resistance or resilience measures
>
> 3. The provision of flood insurance should be equitable
>
> 4. The model should not distort competition between insurance firms
>
> 5. Any new model should be practical and deliverable
>
> 6. Any new model should encourage the take up of flood insurance, especially by low-income households
>
> 7. Where economically viable, affordable and technically possible, investment in flood risk management activity including resilience and other measures to reduce flood risk should be encouraged. This includes, but is not limited to direct Government investment
>
> 8. Any new model should be sustainable in the long run, affordable to the public purse and offer value for money to the taxpayer[10]

The Group raised concerns about the future affordability of flood insurance for those in high flood risk areas, particularly for those on low incomes:

> The Group agreed that the primary problem in the future will be the affordability, rather than the availability, of flood insurance premiums for households and small businesses. There are two main causes of this:
>
> - As the level of cross-subsidy in the market decreases there will be a small benefit for many and a potentially large cost for a few homes at high risk of flooding. There should be further analysis done to quantify the size of these costs and benefits and who receives them.
>
> - Climate change means that the frequency, severity and type of flooding will change. The impact of this flooding on the cost of insurance premiums will depend on both the success of flood defences in preventing damage and

9 Flooding and insurance: a roadmap to 2013 and beyond: An interim report of the flood insurance working groups, Defra, May 2011
10 Ibid, Defra, May 2011

> the extent to which properties are vulnerable, i.e. the number of properties that are built in high-risk areas. Account should be taken of the risk presented by surface water flooding, including how the pattern of future development affects run-off of surface water. The resulting rising costs of repair are likely to create an upward pressure on premiums across the board.

Combined, these effects are likely to result in premium increases for those at the highest risk unless steps are taken to manage exposure. This will be harder to bear for households on lower incomes so further analysis should be undertaken to show which people, and how many, will be uninsured or under-insured as a result.

It is difficult to predict the extent of any problems with availability of cover as these depend on reactions of the market. However, it is far more likely that households will go without cover because they can't afford it than because there is not an insurer willing to provide it.

[…]

The Group has identified several possible secondary consequences of reduced levels of flood insurance. They include mortgageability, and increased economic cost of flooding as well as health and welfare implications. These should be included in any assessment of the value of Government action.[11]

11 Flood risk and insurance: A roadmap to 2013 and beyond: Final report of the flood insurance working groups, Defra, December 2011

4. Agreement at last

Agreement on a way forward was announced as part of the statement on infrastructure spending. At its heart the deal includes

- a commitment by the industry to offer insurance in high risk areas at affordable prices;
- the establishment of the Flood Re scheme run by the industry;
- a guarantee that the government would be primarily responsible for losses due to 'a catastrophic event' that Flood Re could not meet; and
- increased government spending on flood defences.

On 27 June 2013 as part of his speech about infrastructure investment, the Financial Secretary said:

> Too many Members of this House, on both sides, have in recent years seen the devastation that flooding can cause in their constituencies. We need to work with the private sector to protect families from the threat of flooding, so we will provide £370 million in 2015 and increase that in real terms every year to 2020. More than 400,000 households will be protected over this decade. Insurance also has a vital role to play in helping households deal with the consequences when flooding does occur. I am pleased to tell the House that we have now reached an initial agreement with the Association of British Insurers on the future of flood insurance. The industry wants to do the right thing and so do we. We have always said that we wanted to find a solution that works for households at risk of flooding, wider bill payers and the taxpayer. The industry's proposed scheme, known as Flood Re, promises to do that by effectively limiting insurance prices for high-risk households. Up to 500,000 households would be helped, with support targeted towards those on lower incomes. Support would be funded by a levy on insurers, something the ABI has promised us will not increase customer bills in general. Importantly, there will be no cost to taxpayers.
>
> There remain many details to work through, so we propose also to take powers to allow us to regulate for affordable flood insurance should that prove necessary. We are seeking these powers in the Water Bill, which we are today introducing to Parliament. The Secretary of State for Environment, Food and Rural Affairs is today launching a public consultation on our proposed approach, and we welcome views on it. He will introduce our final proposals to Parliament as a Government amendment in the autumn.[12]

More detail on the financial aspects can be found in the accompanying document *Investing in Britain's Future*. It says:

> The risk from flooding continues however. To demonstrate the Government's commitment to managing this, it has set for the first time a specific long term funding settlement for flood defences, rising to £370 million in 2015-16 and then protected in real terms to 2020-21. This provides a total of £2.3 billion and represents a real annual increase of 18 per cent compared with the Spending Review 2010 period.[13]

[12] HC Deb 27 June 2013 c467
[13] Investing in Britain's Future, *p8.25*

The ABI issued the following statement:

> Key elements of the framework are:
>
> Flood Re will be run and financed by insurers as a not-for- profit fund which will cover the cost of flood claims from high risk homes.
>
> Insurers will pass the flood risk element from those households deemed at high risk of flooding to the fund. Premiums for the flood risk will be calculated based on council tax banding up to a maximum limit depending on the Band.
>
> Flood Re would charge member firms an annual charge of £180million.This equates to a levy of £10.50 on annual household premiums and represents the estimated level of cross-subsidy that already exists between lower and higher flood risk premiums.
>
> Flood Re will be designed to fully deal with at least 99.5% of years. Even in the worst half a per cent of years, Flood Re will cover losses up to those expected in a 1 in 200 year – a year six times worse than 2007 – with Government taking primary responsibility – working with the industry and Flood Re – for distributing any available resources to Flood Re policyholders should claims exceed that level.
>
> Providing operational issues, including governance and regulatory approval, are resolved, the aim is for Flood Re to be up and running by summer 2015, with regular progress reviews taking place to ensure Flood Re can proceed. For now ABI members will voluntarily continue to meet their commitment to continue to offer flood cover to existing customers under the previous Flood Insurance Statement of Principles.[14]

The terms of the deal make it unlikely that government would need to contribute funds of any magnitude. Properties built after 1 January 2009 remain uncovered. Insurers guarantee to continue to offer cover to existing customers where flood risk is not 'significant' according to the Environment Agency, or where the Government has announced plans to reduce flood risk below 'significant' within five years.

More details on the agreement can be found on the ABI website here.

The Water Bill

As the statement made clear the scheme was to be taken forward by proposed new clauses to be added to the then *Water Bill*. These can be found in the Department's document Water Bill: commentary on Draft Flood Insurance Clauses and in the follow up document by the Department Commentary on Proposed Flood Insurance Amendments of November 2013. This follows publication of a consultation document in June 2013. Consultation on the draft clauses ended on 20 September 2013. Modified draft clauses were included at the committee stage of the *Water Bill* (Bill 146 2013/14). In a stand part debate on the new clauses the Minister gave a brief summary of some of the important features of the agreement. All quotes are from the Minister, Dan Rogerson, unless otherwise indicated.

Will the system cover small businesses? Yes if they pay council tax:

14 ABI website

> any business based in a property that is primarily a residential property, and on which the occupier therefore pays council tax, will come into the system. Any business based in premises used primarily for business will not be covered. An example might be a farm business. If council tax is payable on the residential property—the farmhouse—that will be covered, but barns and outbuildings, which may be subject to a business rate, will not be covered.[15]

Will the transition from the old system lead to higher prices?

> we want the system to increase incentives for households and communities to manage their flood risk. However, there was a risk that the expiry of the statement of principles could lead to sudden shifts in pricing and cause hardship for those at a higher risk of flood. That is why we are introducing measures to help those at risk in the medium term. We want to ensure that transition takes place in an orderly and equitable fashion. That message emerged clearly from the consultation, so we have strengthened the provisions in that respect.[16]

Will the government face a financial liability if the fund built up by Flood Re runs out?

> there is no Government liability for Flood Re. As I have said before, the UK has a multi-billion-pound, world-leading insurance industry and we believe that it has the ability and the financial strength to resolve this issue without calling on hard-pressed taxpayers[17]

How many properties are likely to be included in Flood Re?

> We anticipate that around 500,000 high-risk households could benefit from the flood reinsurance scheme, and pay less for their insurance than they might otherwise. The price of a high-risk combined buildings and contents policy would be about £720 per year for a band C household. While that might be higher than some high-risk households are paying now, without Flood Re, such policies could be well over£1,000.

Thomas Docherty:

> I want to tease out of the Minister that estimate of half a million. I think this is the first time we have had that figure in front of us. I know that it was not in the letter he helpfully sent me yesterday. Could he say a little more about how that figure of half a million homes was reached?

Dan Rogerson:

> In all these issues, we are guided by those in the industry who have the information at their fingertips. I know that the hon. Gentleman is concerned about the accessibility of that information. That is an issue we will discuss later; it is a good point. Alternative estimates have been made, for instance by the British Insurance Brokers' Association, that were slightly lower. In all of this we have been in discussion with the Association of British Insurers who have the most up-to-date information, and that is where the figure of 500,000 came from. 18, we feel,

[15] PBC 12 December 2013 c236
[16] PBC 12 December 2013 c237
[17] PBC 12 December 2013 c237
[18] PBC 12 December 2013 c239

When will the government step in?

> The memorandum of understanding with the Association of British Insurers sets out that if flooding exceeds a one in 200 year event the Government of the day will take primary responsibility for apportioning money and working with Flood Re and representatives of the insurance industry to ensure that resources are distributed to Flood Re customers.[19]

Will there remain 'uninsurable properties under the scheme?

> I understand from the discussions I have had that the concept of uninsurability will emerge as Flood Re operates, in terms of the numbers of properties affected and the ability to take account of the cases that the hon. Gentleman raises. While there might be estimates of the number of properties that would be in that situation, that point is what we need to remember.
>
> I can confirm to the hon. Gentleman that there are no plans to exclude those at the highest risk at the outset. However, it may be necessary to assess properties that might come into that category as the scheme develops, to establish whether they are flooding repeatedly year after year perhaps, or whatever—those at the very highest risk. When the system begins operating, there will not be that concept of uninsurability.
>
> […] This is an industry-based scheme and so the details of the scheme will develop, but this concept of uninsurability is not there at the outset. However, we must have a means of ensuring that the use of the funds, which after all will be built up by a levy from other payers, is proportionate. We have to deal with that question. We must have a way of considering properties that repeatedly flood and draw disproportionately on the funds of Flood Re.[20]

How is Flood Re funding envisaged to work?

> Insurers that decide to reinsure the flood risk element of a household policy with Flood Re will pay in the premium to Flood Re based on the relevant eligibility thresholds for participation in the scheme, which will be effectively limited to a level lower than the market price for that risk.
>
> By definition, therefore, Flood Re will on average make a loss on every policy it holds. Flood Re therefore needs an additional source of income to fund that loss and to cover its liabilities. That is where the levy comes in. The primary levy captures the existing cross-subsidy insurance market between those at low and high risk of flooding.
>
> The majority of households not at flood risk should not see any increase in their bills due to Flood Re's introduction. The Government have been clear throughout that limiting the impact on household bills was a vital component of the scheme. Flood Re will use the income to settle claims, buy reinsurance and pay for the administration of the scheme.
>
> Subsection (1)(a) of new clause 3 therefore allows the Secretary of State to require all relevant insurers to pay the primary levy. The levy will be set by regulations at a level that would initially equate to £10.50 on each combined household policy in the UK for the first five years of the scheme. However, to facilitate a smooth

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[19] PBC 12 December 2013 c241
[20] PBC 12 December 2013 c241-2

> transition to risk-reflective prices, that and other aspects of scheme funding and eligibility will be reviewed by the Government in consultation with Flood Re at regular intervals during the scheme's 25-year lifespan. It is anticipated that future discussions will lead to decreases in the primary levy and corresponding increases in eligibility thresholds, which will ensure that the policy objective of a smooth transition to risk-reflective prices is being delivered.[21]

How will government review the scheme and its solvency, in the future?

> It is certainly intended that the policy will be reviewed every five years by Government to assess the level at which the levy and the eligibility thresholds are set. That will ensure that the objectives for Flood Re will continue to be delivered, and that includes the transition to a risk-reflective price. Thresholds and the levy will need to be set in secondary legislation, as the hon. Gentleman rightly assumes, so Parliament will have the opportunity to take a view in the normal way as part of that scrutiny process.
>
> […] Joint modelling by Government and the industry suggests that the primary levy, Flood Re's reserves and its reinsurance cover should be sufficient in most years for Flood Re to cover its costs. If Flood Re makes a profit, that will be retained by the scheme and create reserves that, in the first instance, could cover a shortfall. However, given the unpredictable nature of flood damage, there might be circumstances where Flood Re faces a shortfall and does not have those reserves or where losses are below the point at which reinsurance takes effect, such as with consecutive flooding events, or in the early years of the scheme as the reserve builds up. New clause 3 therefore allows for further ad hoc contributions to be sought from all by way of a top-up levy. Subsections (1)(b) and (2) of new clause 3 refer to the top-up levy.
>
> Analysis suggests that top-up contributions should be required, on average, only once or twice in the first 10 years of Flood Re's operation. In those circumstances, Flood Re may be required to call on those top-up contributions urgently in order to remain solvent and to ensure it meets its capitalisation requirements under EU law.[22]

Note: subsequent to this statement, Flood Re estimate that is it "incredibly unlikely" that any reasonably forecastable event would exceed the £2.1billion of reinsurance cover which it already has in place. The costs of even the worst of the recent severe flooding events is "comfortably below" the £2.1billion limit. Hence the measures for 'top up contributions' mentioned in the legislation are largely theoretical.

Will Flood Re affect public finances?

> We expect the Office for National Statistics to classify at least some of Flood Re's funding as public money. That is why it is necessary that these amendments provide the Government with the powers to specify a control framework to ensure the scheme is managed appropriately while respecting that Flood Re needs an amount of operational freedom to manage its business effectively.
>
> Based on current assessments of Flood Re's finances, we will look to prevent Flood Re from incurring net losses of more than £100

21 PBC 12 December 2013 c2413
22 PBC 12 December 2013 c244

million in any one financial year. This, combined with controls preventing borrowing across years, will limit Flood Re's impact on the public finances. I am sure that all Committee members would agree that it would not be acceptable to have an independently managed body that could add to public debt or borrowing without some controls. The industry proposes that insurers should be able to present top-up contributions as member capital to Flood Re, rather than as cash. This capital call could be retained as an asset on insurers' balance sheets, and would not then be a cost to be passed on to consumers.[23]

How will Parliamentary scrutiny be affected?

As far as possible, we want Flood Re to be treated like a private sector body, even though it will be managing public money. We are therefore proposing specific arrangements for Flood Re to be directly accountable to Parliament for its ongoing operations. Clearly, that has novel implications for accountability and scrutiny arrangements, with less direct Government management, oversight and accountability than would be expected for a conventional arm's-length body, and greater direct accountability for Flood Re.

We propose that the relevant Ministers will be accountable to Parliament concerning general policy matters relating to flood insurance, with DEFRA's accounting officer accountable to Parliament for the net expenditure for Flood Re as reported in DEFRA's accounts. However, as an industry-owned and managed entity, Flood Re would be accountable to Parliament for the details of its operations.

[…] I will now set out some of the accountability arrangements, particularly with regard to how the company will be scrutinised.

To provide effective oversight, the clause [new clause 4] provides the Secretary of State with powers to introduce through secondary legislation requirements on accounting, including the role of the National Audit Office in scrutinising Flood Re. The approach has been agreed with the NAO. The NAO will be able to examine the scheme's value for money aspects, propriety and regularity. It will have a right of access to documents and the ability to report to Parliament on its investigations. Flood Re's audited accounts will also be laid before Parliament.[24]

How will the flood insurance obligation work?

The Environment Agency, working with its equivalents in the devolved Administrations, would create a register of those properties at higher risk of flooding. The Secretary of State would set an overall target for the number of registered properties that the industry as a whole needs to cover. Insurers would then be required to provide insurance cover to a proportion of those properties to meet a quota, which is calculated in proportion to their share of the overall market, or risk enforcement action by the Financial Conduct Authority. As a result, insurers will be incentivised to compete with one another to ensure that they meet their quota requirements. We recognise that the obligation does not offer certainty about the cost of insurance in the way that Flood Re does. However, our modelling suggests that the creation of an artificial market for properties at greater risk of flooding will drive insurers to compete with one another to

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23 PBC 12 December 2013 c245
24 PBC 12 December 2013 c247

> provide cover for the properties on the register, which will have the effect of keeping prices down.
>
> New clause 7 puts in place the framework for the obligation. It allows the Secretary of State to require all insurers selling domestic home insurance in the UK to issue insurance policies to meet their quotas. Regulations may make provision for individual insurers to calculate their quotas with reference to a market-wide target set by the Secretary of State, which will mean that each insurer will have to insure its fair share of higher-risk properties. Different targets could be set for different types of insurance risk, such as for buildings and contents cover. That should enable both home owners and tenants to access affordable insurance.[25]

How will government enforce the obligation?

> The approach we are taking is to ensure that all the companies are carrying their fair share of the risk. That is very much the intention, so, as I have said, we need that information from them to be able to look at the size of the market, and then we will be able to see how much each company would need to make to carry its fair share. […]
>
> The Secretary of State may publish that information in order to enable insurers to determine their individual market share. Insurers are required to submit annual returns to the PRA. The information collected relates to household risks. That is not suitable for the purpose of the flood insurance obligation, first because it does not distinguish between buildings and contents insurance policies, and secondly because certain types of firms are not required to provide that information to the PRA.
>
> New clause 10 enables the Secretary of State to provide for enforcement of the requirements on insurers made under clause 9 to provide certain information.
>
> Regulations will allow the Secretary of State to impose sanctions such as civil penalties against those insurers who fail to comply with the requirements to provide information. The regulations would set out the procedures to be followed if sanctions are imposed and could provide for costs incurred in connection with imposing sanctions to be recovered. Insurers would be able to appeal against the sanctions or a requirement to pay costs to the first-tier tribunal.[26]

And:

> New clause 11 provides for the creation and maintenance of a register of properties in the UK that are at greater risk of flooding and are therefore more likely to be experiencing problems with the availability and affordability of flood insurance. The register is essential for the obligation to work properly. Our expectation is that the register will be based on flood risk information held by the bodies with principal responsibility for flood risk management in the different parts of the UK: the Environment Agency, the Scottish Environmental Protection Agency, Natural Resources Wales and the Department of Agriculture and Rural Development in Northern Ireland. New clause 11 also provides for the exclusion from the register for properties built since 2009.[27]

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25 PBC 12 December 2013 c250
26 PBC 12 December 2013 c252
27 PBC 12 December 2013 c253

> *Will the Financial Conduct Authority (FCA) be responsible for breaches of obligation requirements by insurers? Yes.*
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> It is our view that the FCA is the appropriate body to receive compliance reports from the insurers, as it will be responsible for monitoring and ensuring their compliance with the overall flood insurance obligation. The FCA will receive compliance reports from insurers and, under provisions in new clause 16—Functions of the FCA—will be empowered to take enforcement action, should an insurer breach the requirements of the compliance reports.
>
> New clause 16 gives the Treasury powers to apply the FCA's existing supervision and enforcement powers to its new role of monitoring and enforcing insurers' compliance with the requirements set out in new clause 7. Such requirements include issuing a prescribed number of qualifying insurance policies to registered properties at greatest risk of flooding, as set out in new clause 7, and making a report of their compliance or non-compliance with that obligation to the FCA, as set out in new clause 15. The provisions also enable enforcement by the FCA in the case of inaccurate data returns from insurers and late or missing returns where DEFRA sanctions under new clause 10 have been exhausted. The provision allows for the FCA to recover its costs by imposing fees on firms, should that be necessary, in line with its existing practice in wider financial services regulation.
>
> New clause 17 gives the Treasury the power to make regulations requiring the FCA to prepare reports in relation to its role in monitoring and enforcing compliance, as set out in new clause 16. Such reports may contain information about the number of firms that have reported breaches of the flood insurance obligation and the enforcement action that it has taken against them. That information will enable the Secretary of State to review the operation of the obligation and consider whether changes to the level of the overall obligation target are required, ahead of the next compliance period.[28][29]

Why does the new agreement only last for 25 years?

> New clause 20 concerns the proposed lifespan of the flood insurance measures, which we intend to limit to no more than 25 years. We believe that it is right to plan to provide support over that period to smooth the transition to risk-reflective pricing. The approach to managing that transition will be subject to regular review as part of the levy setting discussions. Alongside that, the Government will continue to focus on appropriate controls on spatial planning, maintaining flood defences and other resistance measures and, at household level, protecting properties in higher flood risk areas by encouraging the installation of flood protection measures and resilient repairs after a flood.[30]

Following publication, the extent of the coverage of the new scheme was discussed at length in the Lords stages of the *Water Bill*. Uncertainty over, amongst other things, the position of leasehold properties and business properties persisted. In March 2014 the Department issued an explanatory note on the scope of Flood Re –

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28 PBC 12 December 2013 c255

29 These clauses were implemented as sections 79 to 81 of the *Water Act 2014* however it would appear that the Treasury has not yet (March 2017) exercised its powers under the Act.

30 PBC 12 December 2013 c257

Water Bill: Part 4 Flood Insurance Scope of Flood Re. Which provides the best guide to what is and what is not in scope. The general conditions for inclusion are set out below:

> The definition of "household premises" will be set out in the secondary legislation provided for by clause 69 of the Water Bill. The criteria that the insurance industry will use to distinguish between domestic and commercial policies for Flood Re are:
>
> 1. Properties are insured in the name of an individual or in a trust for an individual;
>
> 2. Properties have a Council Tax band;
>
> 3. Properties are used for residential purposes;
>
> 4. Properties have an individual premium; and
>
> 5. Properties are occupied by the policyholder or their immediate family.
>
> In addition to meeting all of the criteria above, the property must be within Council Tax Bands A-G (or its equivalent in the Devolved Administrations) and must have been added to the Council Tax valuation list (via a Notice of Completion) before 1 January 2009. Any existing property that has been converted to residential use after this date (for example a commercial building being converted to residential use) would not be eligible for Flood Re.[31]

Amongst the categories of homes *excluded* are:

> The following types of properties are primarily out of scope because they are **not insured in the name of an individual** or **under an individual premium**:
>
> Mixed use properties – for example:
>
> - A block of residential flats with shops or businesses on the ground floor,
> - A block of residential flats with some individual flats being used as a business address.
> - Large commercial residential buildings portfolios, such as social housing, Housing Association properties, retirement homes

Hence a charity owned property rented out as social housing might be excluded, but only if the insurance responsibility was left with the charity. If the responsibility lay with the leaseholder then it could be within scope.

More detailed conditions for inclusion are set out here:

> Owner-occupied residential freehold properties (apart from properties in Council Tax Band H or their equivalents or properties built after 1 January 2009).
>
> Owner-occupied residential leasehold houses or bungalows
>
> *Leasehold houses or bungalows that are insured via an individual residential policy, by the leaseholder or their immediate family would meet the criteria and would be in scope.*
>
> Owner-occupied residential leasehold flats, provided that:

31 Water Bill: Part 4 Flood Insurance Scope of Flood Re

the terms of the lease specify that each dwelling purchases its own buildings insurance (currently, a very small proportion of domestic leaseholds fall into this category); or

the buildings policy covers a block of three flats or fewer, and the freeholder(s) lives in one or more of these flats. This means that small blocks (for example converted Victorian homes) where the owners of the flats share the freehold, or where one of the flat owners is the freeholder, will be eligible.

Owner-occupied residential commonhold flats

Sheds, garages and summerhouses

- Most domestic policies would cover outbuildings such as sheds, garages and summerhouses and are therefore in scope (this would be set out in the definition of 'Buildings' within the policy documentation).
- However, large outbuildings which are covered under a separate non-residential policy, such as farm barns, would be ineligible.

Farmhouses

- Provided that the policyholder or immediate family lives there and the rest of the above criteria are met.
- If the farmhouse was included in a commercial policy for a large commercial operation, it would be out of scope. There may be cases where two policies are held on a farm, one covering the residential risk of the farmhouse, and one covering commercial risks, and here the insurer could cede the domestic policy to Flood Re.

Bed and Breakfasts (B&Bs) with a Council Tax band

- Under circumstances where a B&B pays both Council Tax (or the equivalent) and business rates, it would hold two separate policies. The B&B would be eligible for Flood Re for the policy that is residential and ineligible for the policy that is commercial in nature. However, it is not anticipated that many B&Bs would hold two separate policies.

Residential buy-to-let home that has not yet been rented out

- Once rented, a property must be covered by landlord insurance, which is out of scope. Note that a property purchased with a Buy-to-Let mortgage can be covered by domestic home insurance up until the point at which it is rented.

Owner-occupied static caravans

- A static caravan would be eligible provided that it is covered by a domestic insurance policy.

Unoccupied properties, provided they are for residential use and have a Council Tax Band (apart from those relating to properties in Council Tax Band H or their equivalents or properties built after 1 January 2009).[32]

The relevant parts of the *Water Act* that bring Flood Re into force became live from January 2015.

[32] DEFRA Water Bill: Part 4 Flood Insurance Scope of Flood Re

5. Detailed Regulations

Most of the detailed rules for the Scheme were left to subsequent regulation. Defra published its consultation on these in July 2014 – The Flood Reinsurance Scheme – Regulations.

The Consultation covered a variety of issues including definitions of things such as 'flood'; the management of the scheme; its accountability to Parliament; the extent of the public sector's liability for the scheme's funding shortfalls; and its wind down over its intended 25 year lifespan.

The biggest issue initially was the government accounting treatment of premiums and their contribution to government borrowing figures.

A Financial Times article disclosed that the Department of Environment wished to stop Flood Re "from adding more than £100 million to public sector borrowing in any given financial year.[33] The Office of National Statistics (ONS) will classify the premium on all policies as a tax.[34] For the first five years this levy is set at a maximum of £180 million.

5.1 Consultation Response

The consultation response was published in December 2014.[35]

In most respects the proposals reflected in the Act and the consultation were agreed to. However, some changes were made, some of policy and some merely definitional, and it clarified some of the questions which industry and the public had sought information on.

Government responsibility

For example the Government made a point of highlighting the fact that Flood Re is not forever:

> In response to comments about the 25 year length of the Flood Re Scheme; the length of the Scheme is designed to provide a smooth transition to risk reflective pricing for those policy holders at high risk of flooding. It is intended that the Scheme protects those most vulnerable to a potential increase in the cost of flood insurance in the shorter term, while helping prepare those households for the management of risk in the medium to long term. The period of operation of the Scheme is set in the Water Act 2014 and reflects all consideration of this issue made at that time.[36]

It also explained what would happen if there was the catastrophic more than 1:200 year loss event (where the flooding was six times worse than the 2007 floods:

> Should flooding occur on a scale greater than this [1:200 event], Flood Re and the Government will decide how to best respond, as

33 Financial Times; *Flood insurance scheme 'unworkable', say insurers*, 22 July 2014
34 Consultation document pp38
35 DEFRA; Govt response to the public consultation on the Flood Re Scheme Regulations; December 2014
36 Govt response to the public consultation on the Flood Re Scheme Regulations p10

> part of a wider response to what would be a national emergency. We cannot set out what actions would be taken with regard to Flood Re as such decisions will be for the Government of the day. However, we have been clear that Flood Re does not retain any contractual liability in such a scenario, which will pass back to insurers who will continue to pay out claims in line with the terms of the insurance policy.[37]

Flood Re financing

There were adverse comments by the industry on the financing of Flood Re:

> Several insurance companies felt that the restriction on Flood Re's ability to add more than £100 million to the public sector net borrowing (PSNB) is too restrictive, because of uncertainty about the cost of reinsurance for Flood Re. It was felt that if these costs were too high; this could absorb most of the Primary Levy and premium income thereby reducing the rate at which Flood Re's reserves built up, impacting the rate at which the Primary Levy needs to be set. Insurers also wanted greater clarity on how Flood Re would capitalise itself at the Scheme's inception.[38]

The Government's response to this was:

> The consultation made clear that the restrictions on Flood Re's ability to add more than £100m to the PSNB was an area of ongoing dialogue with the industry. We have worked intensively and constructively with Flood Re and the ABI and have agreed that protection for public expenditure should instead be provided by the purchase of appropriate reinsurance. Therefore Flood Re's Articles of Association will include a provision, the effect of which will require that the Flood Re Scheme Administrator must purchase appropriate stop-loss reinsurance (or equivalent cover with the same effect) so that the Scheme does not have an impact on PSNB greater than £100m (the "loss limit") at the end of any one financial year.
>
> In order to ensure that this limit cannot be changed the Government will take on a limited membership role in Flood Re itself. This will also allow Government to be able to veto the ratification of any amendment to this Article, although we have been clear that we do not expect Government to have a wider role in the day-to-day running of Flood Re, in keeping with the industry run and managed nature of the Scheme. The details of this are to be finalised.[39]

And

> In relation to Flood Re's initial capitalisation, we have been advised by Flood Re that the industry's preferred approach to adequately capitalise Flood Re in the initial period is through a Levy II capital call. This is necessary so that Flood Re is solvent and to meet requirements set by the financial regulators. In normal circumstances, such a call would trigger a review of the Scheme, however we have amended the Regulations to allow for this, exempting Flood Re from triggering a review as it capitalises itself in year one. Because of the nature of the call, we do not expect this to impact on household bills and have sought assurances from the industry to this effect. More widely we have also

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37 Govt response to the public consultation on the Flood Re Scheme Regulations p22
38 Govt response to the public consultation on the Flood Re Scheme Regulations; p10
39 Govt response to the public consultation on the Flood Re Scheme Regulations; p11

> introduced a new provision to make clear that nothing in the Regulations either prevents or requires Flood Re to pay back Levy II contributions, further safeguarding householders against increases in the cost of home insurance as a result of the Levy II mechanism.
>
> We have also considered the issue of borrowing further, and do not believe it would be appropriate to completely limit borrowing on behalf of Flood Re. In order to operate as a normal insurance company, Flood Re will need the ability to borrow certain amounts in the normal course of its business. We have revised our approach so that Flood Re is able to carry some borrowing over financial years, up to a limit of £25m. The interaction between this figure and the "loss limit" will be confirmed as part of the review three months prior to "go-live". **We have amended the regulation to make clear that normal transactions relating to reinsurance will not be captured within the definition of borrowing for these purposes; however it will include sums owed to trade creditors and other commercial borrowing**.[40]

Changes were made to the way in which insurers' shares are to be calculated (pp58) and the exemption for new insurers will be tightened to ensure that existing businesses are not hived off as 'new' and the definition of 'relevant insurer' is amended to ensure it includes Lloyd's members.

Leasehold properties

A number of further definitions, of things like 'household premises' were amended following consultation. It confirmed that 'properties that are rented out will not be included' (pp78).

Although the consultation was about the forthcoming regulations, 134 responses to it were focussed on the exclusion of leasehold properties and other 'out of scope' issues. The Government's response in full is shown below, however, the big change is that properties in Band H of Council tax will no longer be excluded:

> 105. We have considered carefully the concerns raised through consultation responses and via workshops and meetings. We have been clear that contents insurance will remain available for leasehold properties. There remains insufficient evidence of a systematic problem with leasehold buildings covering more than three residential units. Therefore there have been no changes to the policy on the leasehold sector; except that some leasehold flats are no longer expected to contribute towards Scheme funding (these particular flats remain eligible for Flood Re). More information on this change has been set out under Question 7 above.
>
> 106. The position on the inclusion of small businesses has not changed. Overall there is insufficient evidence to justify Government intervention in the provision of insurance cover for small businesses. Flood Re has been designed to cover the domestic rather than commercial sector. However, we recognise the challenges that some small businesses could face in areas of high flood risk. We have committed to work with the ABI and other stakeholders to monitor the insurance market for small businesses and consider the issue with the industry if the situation were to change significantly.

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40 Govt response to the public consultation on the Flood Re Scheme Regulations; p12

107. We have considered the concerns raised about the impact on households in Band H properties of paying towards the Scheme and facing high insurance premiums in flood risk areas. The insurance industry has provided assurances that the inclusion of Band H properties would not affect the £180 million Primary Levy on the industry and that properties in lower Council Tax bands would not be subsidising Band H properties. **The Government has agreed that provided these conditions are met the policy can be changed and Band H properties will now be eligible for Flood Re**.

108. The cut-off date for eligibility for Flood Re will remain 1 January 2009, in order to maintain consistency with the Statement of Principles and avoid any potential incentives to build homes in areas of flood risk.

109. The position remains that it would not be appropriate for Flood Re to provide cover for landlord insurance, which is more extensive than standard home insurance, with at least some elements of commercial insurance included. We have been assured by the industry that the majority of landlords would be able to find a more competitive rate outside of Flood Re. Contents insurance will remain available through Flood Re for tenants of rented properties.

110. There were several questions about eligibility for various forms of property rental. In general, properties rented on a permanent basis are not eligible for Flood Re. No properties where the insurance cover is commercial in nature are eligible for the Scheme.

111. A number of questions were asked about specific scenarios on property rental and the answers are set out below:

- • A room which is rented out under the 'Rent a room Scheme' would not mean the property is excluded as the policy holder still lives in the property and would be able to take out a domestic home insurance policy.
- • If the tenants of a property move out, its insurance policy is only eligible provided a domestic policy is taken out in the place of the commercial landlord insurance; once the property is covered by landlord insurance it becomes out of scope again.
- • If a family home is rented out for a short period , or as a holiday home, and covered for that period by landlord cover, it would be out of scope for that period, but would come back into scope provided domestic insurance is reinstated once it returns to family use.[41]

[41] Govt response to the public consultation on the Flood Re Scheme Regulations; p21

6. Commencement

The paving legislation for both the scheme and the scheme administrator can be found in two Sis:

The Flood Reinsurance (Scheme and Scheme Administrator Designation) Regulations 2015.

The Flood Reinsurance (Scheme funding and Administration) Regulations 2015.

Upon publication of the draft legislation, the ABI commented that:

> Flood Re welcomes the news that the secondary legislation that defines how Flood Re will operate has today been laid before Parliament by the Secretary of State for the Environment, Food and Rural Affairs, Elizabeth Truss.
>
> **Brendan McCafferty, Chief Executive Officer, Flood Re** said:
>
> "Laying the secondary legislation is a highly significant milestone on the path to the establishment of Flood Re. It marks the completion of negotiations with Government, allowing the legislative process to be completed after the election, and is the result of many months of very detailed work between Flood Re, the industry and Government. The regulations provide the certainty necessary to allow us to move into the build and test phases of Flood Re's development.
>
> Flood Re is the first scheme of its kind in the world and is a highly complex undertaking. The laying of the regulations is an important step towards enabling affordable insurance to be available for those households and families most at risk of flooding."[42]

In June 2015 however, it was announced that the launch had been postponed till April 2016. A spokesman for the Scheme commented:

> "We are planning to go live with [Flood Re] in April 2016. The permanent executive team which was appointed last September has never commented publicly about when Flood Re will launch.
>
> He continued: "Flood Re is a complex scheme which needs to be tested thoroughly if we are to get it right first time for UK home insurance customers.
>
> "Building Flood Re's systems and infrastructure is on track and will be established in the summer as previously indicated. However, being ready to launch for consumers requires extensive testing that needs to be done with 300-400 insurers. That is a complex and lengthy process which requires a realistic timeframe."[43]

The initial reinsurance agreement, "an important milestone" was announced on 2 February 2016 by Flood Re:

> Flood Re has successfully secured a £2.1 billion multi-year reinsurance programme. In an oversubscribed second phase of the tender process, Flood Re successfully bound the additional capacity required to complete the placement. The three year

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[42] ABI Press Release

[43] Reported Daily Telegraph; *Government insurance scheme launch confirmed for 2016*; 8 June 2015

> programme is one of the five largest 'natural peril' reinsurance deals struck globally and the second biggest in Europe.
>
> The second phase saw 45 entities offer capacity to meet the required amount to complete the programme, with 38 of those parties ultimately securing a share of the placement. In phase one, which concluded in late 2015, some of the industry's leading reinsurers collectively offered nearly £1.29 billion of multi-year coverage – with leaders Munich Re and Swiss Re contributing very significant support.[44]

6.1 Flood Re in practice

In time it will become clearer how effective the scheme has been. One year after it came into force inevitably what has risen highest in the coverage are cases where the scheme has not provided great solutions. This might be excessive expectations of what it would do – flood affected properties are liable to have higher premiums regardless of Flood Re.

An article in the industry magazine Post in March 2017 reviewed the industry's views on how it has worked coming up to a year on.[45] According to the article, the insurance company Aviva has seen 11,000 new policies as a direct result of Flood Re and Axa 1,800. In total Flood Re "is on track to back 130,000 new policies". It continues, "60 insurance providers were now on board, representing 90% of the home insurance market."

On the anniversary of it coming online Flood Re issued the following notice:

> Prior to launch, Flood Re commissioned a benchmarking exercise to examine the impact on availability and affordability of flood cover. The research by Consumer Intelligence, a specialist in customer satisfaction and insight in the financial services sector, showed:
>
> - Before the introduction of Flood Re, only 9% of householders who had made prior flood claims could get quotes from two or more insurers, with 0% being able to get quotes from five or more.
> - In the scheme's first month in operation, this number rose dramatically to 68% of these households being able to get quotes from five or more insurers.
> - By December 2016, this increased further so that 84% could get quotes from five or more insurers while 95% could get quotes from two or more.
> - Currently, 58% of those households that had previously made flood claims now have access to ten or more quotes.
>
> At launch, 16 insurance providers were signed up to the scheme and this has now increased to 60 insurers. They represent 90% of

44 Flood Re press release 2 February 2016.
45 Will Kirkman, Post Magazine; Flood Re: One Year on – how effective and successful is the scheme?

> the home insurance market which means that Flood Re has changed the market by enabling consumers in flood-prone parts of the country to have more choice.
>
> Since the introduction of Flood Re, the data shows four out of five householders with previous flood claims saw a reduction in the price of available quotes of more than 50%.[46]

In general the industry is full of praise for how policies have been moved into Flood Re – "a seamless process". It is claimed that it is good for the public too. A representative of Aviva said that "customers save around £500 per year in premiums on average". In the case studies on the Flood Re website, there is an emphasis on the reductions in the excess imposed on households liable to flood. In some cases from £tens of thousands to a few £hundreds.

A dissenting view was given by an academic who argues that Flood Re reduces the incentives on government to manage flood risk and on homeowners to do more to flood proof their properties. It was, she said a "stop gap" which deflects effort away from the true problem of flood resilience.

This appears to be a minority view though. The Chairman of Flood Re, the previous Conservative Minister Mark Hoban, notes that government spending on flood defence has increased since the scheme began and that the scheme "creates a body that advocates for (flood) defences" backed up by the data available to them from their members.

The first Report and Accounts of Flood Re (y/e March 2106) can be found here.

6.2 Outstanding Issues

There are two areas where the problems of availability and price of insurance have not yet been solved. The first is for (mainly) small firms and the second is for blocks of leasehold premises (flats) above the Flood Re threshold of three properties.

Commercial/ small firms

Flood Re applies to the domestic insurance market only. The insurance industry says that the commercial market works well and that there is no problem to solve there.

During the winter of 2015, flooding affected many northern regions of England. Many businesses were affected and found, in the aftermath, that either flood cover was withdrawn or the excess/premium had increased to such an extent that it was commercially unviable.

An adjournment debate was held on this subject on 8 February 2016.[47] The Minister, Rory Stewart, outlined the arguments against a commercial Flood Re equivalent.

> First, setting up one of these schemes involves a very considerable cost to the dry. […] For example, if a business has indeed, as he

46 Flood RE website 4 April 2017
47 HC Deb 8 February 2016

> said, flooded twice in four years at a cost of £500,000 to its stock each time, it will be difficult to provide insurance without some measure of cross-subsidy for businesses that are not in flood-affected areas.
>
> The second problem is the complexity of flood insurance for businesses. It is much more straightforward for householders, […]. A business, on the other hand, has to look at how much it […] wants to lower its premiums and self-insure against a higher excess. […] An internet company will not want to invest much in insuring the building that it is in, whereas for a farm, a property business or a restaurant, that fixed structural asset is absolutely essential to the continuity of its business.
>
> […]
>
> There is also, of course, the issue of moral hazard. We do not want to encourage businesses to locate themselves in flood-vulnerable zones if they have a high fixed structural asset cost. […] Nevertheless, something must be done. […]
>
> Thirdly, should we consider a different insurance model? One possibility—we have not done this in flood insurance before—is to consider the approach taken by travel and medical insurance, which have a fixed indemnity. If the Government are to be involved, it might be reassuring for them to know that a property had a fixed indemnity of £20,000 or £50,000 attached to it, rather than what we have at the moment, which is an unlimited flood insurance liability.[48]

The Minister said that he was going to discuss the problem with the industry.

An article in the insurance industry trade magazine, *Post*, confirmed that an industry government roundtable had taken place but that a Flood Re scheme for SMEs was "fundamentally challenging".[49]

Issues identified as challenges included

- the smaller population from which to draw the subsidy;
- which businesses would be in the same 'pool' to provide for and claim on subsidies and pay flood premium levies (would all the hairdressers be in the same 'pool');
- the ethics of business subsidies; and
- business claims vary more widely than claims for homes – because they will include elements for business interruption.

The article noted that a survey by the Federation of Small Businesses found that only 6% of SMEs in at risk areas had failed to find insurance and only 3% had been offered it but found it unaffordable.

The insurance industry magazine – *Insurance Post* – reports on progress on help for small businesses:

> […] in December [2016] , the British Insurance Brokers Association launched a scheme for small businesses excluded from Flood Re.

48 HC Deb 8 February 2016 c1414
49 Post Magazine; SME flood scheme 'challenging to implement despite government talks; 18 February 2016

> Underwritten by Lloyd's … the new product is available to BIBA members.
>
> Ian Fletcher, director of policy at the British Property Federation, sees no issue with the scheme being limited to BIBA brokers. "In practice, most leasehold business, I suspect, would be placed via a broker and since most brokers are members of BIBA, it should mean easy access to their scheme". In the private rented sector, more business is done direct with insurers rather than via brokers,. "But if you are struggling to get flood cover, you would have access to a broker and in most cases want their help, so overall this is a good scheme that would help the people we represent".[50]

In a presentation to the APPG on flooding, a representative of BIBA said that "We are aware that since the Statement of principles was withdrawn the flood insurance market for SMEs has been contracting, as some insurers leave the market, or provide quotes excluding flood cover, which introduces pressures on the scheme." It said drew a strong link between affordable premiums and extra spending on resilience by both businesses and the government.

Leasehold flats

Many members have received complaints from constituents that because they live in a block of leasehold flats they cannot get affordable insurance. In some cases modest properties have quotes for insurance of £10,000's and excesses almost as much as the cost of the property itself.

This issue was raised during a Westminster Hall Debate in December 2016 designed to highlight the problems of these groups, produced this response from the Minister Dr Coffey:

> Turning to leaseholds, particularly long leaseholds, I have commissioned my officials to look at the nature and extent of the problems that my hon. Friend the Member for Carlisle described, as we need to look at them in more detail. He will be aware of the wider issue of small leasehold property, to which he referred. The insurance industry regularly informs us that for, the most part, affordable commercial insurance and contents insurance for individual leaseholders is available through Flood Re, but there are examples of individuals and leasehold properties with more than three residential units struggling to access affordable business insurance. Likewise, there are examples of residential buy-to-let properties not being covered and owners finding it difficult to obtain insurance.
>
> Evidence is building and the challenge is not easy. Much consideration was given during the creation of Flood Re to whether to include leasehold properties. From a practical perspective, insurers determine whether an individual property is at high flood risk on a household-by-household basis and can allocate the cost using a simple domestic insurance model. For leasehold properties, buildings insurance will often cover

50 *Insurance Post*, January 2017, p44

> numerous dwellings, which may well have different levels of flood risk. It would be difficult to establish a consistently fair approach to how lessees should cover that risk.[51]

6.3 Further information

Flood Re has its own website now. May questions that Members or constituents might have are covered simply on its FAQ pages which cover:

General enquiries

Funding

Eligibility

Guidance

[51] HC Deb 6 December 2016 c55

7. How can flood-related insurance premiums currently be reduced?

7.1 Property-level measures

Property owners can directly reduce the implications of flooding by adopting two types of property-level measures:

- Resistance measures that keep water out of properties, such as air brick covers
- Resilience measures that reduce the damage caused when water enters a property, such as water-proof wall plaster

More information about these measures can be found here and here. Insurers might be willing to reduce premiums once such measures are in place, although homeowners should liaise with their insurer as there is no guarantee that they will do so.[52] The Environment Agency recommended:

> Preparing your property for flooding will limit the distress and damage caused by it, which means less costly repairs AND less time out of your home or business premises.
>
> The cost of purchasing and installing products to keep floodwater out of your property will depend on the size of your property and the type of flood you want to protect against.
>
> For example, according to the Association of British Insurers (ABI), to protect your property against shallow flash floods could cost between £2,000 - £6,000. To keep water out during periods of prolonged flooding will take bigger changes and could cost between £20,000 - £40,000.
>
> Therefore, if there is a high risk of flooding to your property, you may want to consider one of the following:
>
> Property level flood protection funding - We have made funding available to some local authorities and local Environment Agency teams to undertake flood surveys of properties in high risk areas, where the provision and installation of household flood protection measures may also be funded. More information about the scheme can be found on our Property level flood protection funding webpage.
>
> Contact your landlord if you're a tenant, to discuss flood protection options and your willingness to put in place and maintain any barriers.
>
> If your home or business has been flooded or you're doing renovations, repair it so that it's more resistant to flood damage. Speak to your insurance company about repairs that will reduce the damage from future flooding, and possibly reduce excess charges or premiums too.
>
> Check with your mortgage provider to see whether your mortgage can be extended to cover the cost of making your

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[52] Flood risk and insurance: A roadmap to 2013 and beyond: Final report of the flood insurance working groups, Defra, December 2011

> property more flood-proof (provided you have sufficient equity in your property).[53]

7.2 Flood defences

New flood defences can also reduce flood risk and therefore insurance premiums. The new funding arrangements for flood defences mean that local communities can contribute to flood defence works that might not otherwise go ahead. See the standard note on flood defence for more information.

However, it is recognised that improved flood risk is not always taken into account by insurers. This can be because of a lack of detailed local information on risk.[54] The Environment Agency and Association of British Insurers (ABI) stated that supplying insurers with more information could lead to reductions in premiums:

> You should speak to your local Environment Agency office to see if they have any more detailed information that may be able to qualify the National Flood Risk Assessment – for example maximum anticipated flood water levels which can be compared to the actual floor height of your property.
>
> You may be able to supply your insurer with information specific to your property that shows that the flood risk to your property is less than that applying to the area where it is located for example
>
> • You may have better topographical information to demonstrate that your property is higher than maximum anticipated flood levels
>
> • You may be able to demonstrate that all occupied areas of the house are situated above these known levels
>
> • You can show that your community or you have taken individual action to stop flood water getting into your property or to reduce the damage if it does get in.
>
> • You can consider asking an independent professional (for example members of an appropriate chartered institution such as the Chartered Institution of Civil Engineers, Royal Institution of Chartered Surveyors, Chartered Institution of Water and Environmental Management or the Association of Building Engineers), who is experienced in assessing flood risk for individual properties, to assess the flood risk specific to your property.
>
> The Environment Agency is the lead authority in flood mapping and risk assessment, but has no role in determining insurance cover or setting premiums – that is a matter for insurers. However the Environment Agency will take account of evidence from others on flood risk when updating their maps, so please share any information provided to your insurer with your local Environment Agency office. Call the Environment Agency's 24 hour Floodline on 0845 988 1188 or National Customer Contact Centre on 08708 506506 (Mon to Fri 8am to 6pm) or e mail enquiries@environment-agency.gov.uk[55]

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53 Coping with the cost, Environment Agency, viewed 18 January 2012
54 Flood risk and insurance: A roadmap to 2013 and beyond: Final report of the flood insurance working groups, Defra, December 2011
55 Flooding information sheet, Environment Agency and Association of British Insurers, June 2009

Defra, the Environment Agency and the insurance industry are currently working to improve the consideration of local flood risk information in insurance.[56] See here for more information.

[56] Flood risk and insurance: A roadmap to 2013 and beyond: Final report of the flood insurance working groups, Defra, December 2011