Insurance Europe key points for insurers regarding natural catastrophes in Europe

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Introduction

Insurance Europe welcomes the opportunity to issue its key points of concern in relation to the European Commission's plans to issue a Green Paper on natural catastrophes. Insurance Europe fully supports the Commission's work on exploring this topic and stresses that a focus should be placed on increasing the knowledge about Member State risk profiles and exposures as well as on the insurability of natural catastrophe risks.

Naturally, the collection and sharing of this information can help prepare against natural catastrophes and minimise their impact **without damaging currently well-functioning insurance systems**. The variety in risk exposures due to regional environments, level of public awareness about potential risks, extent of government intervention (ie solidarity funds) and practice of adaptation measures (eg flood defences, building codes, sewage back-up systems), demonstrates that no "one size fits all" scheme for the EU is appropriate. Rather, a minimum harmonisation approach – with a focus on best practices to improve the insurability of risk – should be considered if any legislative action is contemplated.

Basic Principles of Insurance

Insurance Europe respectfully suggests that the Commission integrate the below key points into its Green Paper and related study.

I. It must be understood that the conditions for insurability *do not consist of a strict formula*, but rather a set of basic criteria which must be fulfilled in order for the risk to be insurable.

- Randomness – The time and location of an insured event must be unpredictable and the occurrence must be independent of the will of the insured (it should be noted, however, that **not all risks are insurable** and that some losses may be too large for the insurance industry to cover alone).

- Quantifiable – The frequency and severity of the event must be estimated and quantified within reasonable parameters.

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- Mutuality – It must be possible to build a risk pool in which the risk can be ***shared*** and ***diversified*** at economically fair terms to insurance customers (there is a specific need to prevent disproportionate risk scenarios leading to **adverse selection** and/or **moral hazard)**.

- Economic viability – To ensure the financial capability of insurers in offering adequate cover, premiums must not only be appropriate to pay out claims, but to also acquire and administer the insurance business as well as provide sufficient returns on capital to investors.

II. There exist three core principles for improving the effectiveness of the cover of natural catastrophe risks.

- Responsibility sharing – All stakeholders do their part in minimising the damaging effects of natural catastrophes, including government, private companies, insurers and the public.

- Coordinated action – Governments can coordinate with insurers by creating public-private partnerships (ie where governments provide financial assistance to help lower the cost of the available insurance in high-risk zones) or by enforcing collective and/or individual use of structural and/or non-structural measures to help lower the level of risk (ie ***preparedness*** and ***prevention***, particularly through adaptation).

- Ex-ante financing – the EU should support ***coherent Member State frameworks*** that limit public reliance on state intervention (eg emergency funds) as a ***last resort***, so that *ex-ante* financing schemes like insurance - which often pay out claims more **efficiently, quickly and adequately** based on the prediction of risk – can continue to grow.

Key Points for Consideration

Based on the above, Insurance Europe suggests that the European Commission's upcoming Green Paper address the following solutions:

- **Promotion of, and investment in, *forward-looking, multidimensional risk models*, which will assist in further development of the currently available insurance cover.**
    - These models should consider climatic, socio-economic, geological and hydrological data in addition to the basic need for risk mapping.
    - The risk models should be consistent in their methodology, types of data and use of hypotheses in order to facilitate accurate comparisons of risk exposures between Member States.
    - Further investment in the 'Clearinghouse Mechanism' is warranted (eg improving the web-applications hosted on the Commission's website, coordinating with the upcoming EU Adaptation Strategy and focusing on comprehensive qualitative and quantitative information).
        - This should encourage, in parallel, the development of **national clearinghouse mechanisms** at Member State level to enhance the collection and sharing of information about risk exposure, records of natural catastrophe losses, risk reduction measures and the geographic *and* governance issues involved.

- **Foster an environment of *free and ready access* to risk data at both the EU and Member State levels.**
    - Coordinate and disseminate risk data that can be ***easily interpreted and integrated*** into the decision-making process of the public and/or private stakeholders to build their risk awareness.

- Facilitate the sharing of risk data between EU Member States ***without fear of data protection violations*** so that insurers can continue designing appropriate insurance cover.
- Encourage the development of proprietary risk-hazard zoning tools, such as those recently developed by some insurance associations for floods (eg ZÜRS in Germany, FRAT in the Czech Republic and SIGRA in Italy).
- Focus on the improvement of geo-data availability, which is well suited to modelling claim scenarios, to help make a rapid assessment of losses and assign skilled personnel to the site of a natural disaster.
- Encourage the ability to publish public data, such as has been done in cooperation between insurers and governments in some Member States (eg HORA in Austria, the Environment Agency and ABI agreement for public data in the UK, Mission Risques Naturels in France).

- **The Commission should continue to encourage the adoption of national adaptation and prevention policies in view of the increasing effects of climate change.**

  - Governments can facilitate the implementation of adaptation measures via tax incentives for private business or the enforcement of adaptation regulations/codes for people in high-risk areas.
  - ***Preparedness*** for natural catastrophes can be achieved by the implementation of adaptation measures (eg strengthening buildings against windstorm and earthquakes or developing structural barriers against floods and the overflow of rivers).
  - ***Prevention*** is also exercised through adaptation measures, which helps to minimise the impact of natural catastrophes (eg flood defences and building codes aimed at minimising flood or earthquake damage, sewage back-up systems aimed at preventing overflows caused by severe storms).
  - National policies for building/zoning plans must also be given priority in order to stop development in high-risk areas or to otherwise offer the public in high-risk areas more appropriate protections against natural catastrophes. The absence of a **proper planning policy** can weaken the effectiveness of a natural catastrophes insurance system.
  - Adaptation efforts must be flexible enough to adapt to the ***future*** **climatic situations** posed by the expected rise of extreme weather conditions and increasing frequency of natural catastrophes.

- **Government intervention (eg promise of ex-post financing from the state) can be necessary in some cases but should be minimised so as to encourage the uptake of insurance, preparedness and prevention measures (ie adaptation).**

  - Political promises of compensation to the public, without any guidance through national law or regulations, may be counterproductive to raising risk awareness and building the appropriate level of demand for the take-up of insurance.
    - A lower demand for insurance can result in a distortion of insurance availability and insurance pricing, as the amount of people with insurance will not reflect the true amount of people at risk.
  - These promises further diminish public incentive and interest in seeking additional protection via investment in adaptation measures.
  - As mentioned above, some losses may prove to be too large for insurers to cover, in which case a form of government intervention may be appropriate.

- **The EU policy framework concerning natural catastrophes should be flexible for Member States needs and:**

    - ***encourage market-driven initiatives*** so that insurers can continue to build adequate cover for each Member State;
    - ***permit risk transfer mechanism to adapt*** to the local conditions (eg type and severity of risk exposure, cultural attitudes toward risk and level of government intervention); and
    - ***be based on minimum harmonisation*** in order to preserve the different market geopolitical situations that exist today.

Conclusion

Issues of ***risk awareness, free and available risk data, stakeholder cooperation, adequate building planning and the promotion of adaptation and prevention measures*** are core areas that must be improved in order to increase the insurability of natural catastrophe risks, thereby enhancing the effectiveness of insurance in Europe overall. If legislative action is contemplated at the EU level, a more "principles based" approach should be considered as a means of developing best practices for the variety of natural catastrophe insurance needs throughout Europe.

Insurance Europe looks forward to continued cooperation with the European Commission on this matter and extends itself as a resource for the Commission's on-going work in support of its upcoming Green Paper on natural catastrophes.