

Environment, Food and Rural Affairs Committee

Oral evidence: Future flood prevention, HC 115 Wednesday 15 June 2016

Ordered by the House of Commons to be published on 15 June 2016.

Written evidence from witnesses:

- [Brendan McCafferty, Chief Executive Officer, Flood Re, and Mark Hoban, Chairman of the Board of Directors, Flood Re](#)
- [Huw Evans, Director General, Association of British Insurers \(ABI\)](#)
- [Iain Hamilton, Head of Pricing and Underwriting, UK General Insurance for Personal Lines, Aviva](#)

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Members present: Neil Parish (Chair); Jim Fitzpatrick; Dr Paul Monaghan; Rebecca Pow; Ms Margaret Ritchie; Angela Smith; Rishi Sunak

Questions 326-472

Examination of Witnesses

Witnesses: **Brendan McCafferty**, Chief Executive Officer, Flood Re, and **Mark Hoban**, Chairman of the Board of Directors, Flood Re, gave evidence.

Q326 Chair: Welcome very much to you both to our inquiry into flood resilience and flood protection. Today we are particularly interested in Flood Re. I do not think you necessarily need much introduction but if you would both like to introduce yourself we will then move on.

Mark Hoban: I am Mark Hoban. I am the Chairman of Flood Re.

Brendan McCafferty: I am Brendan McCafferty and I am the Chief Executive of Flood Re.

Q327 Chair: How is Flood Re affecting premiums and excesses for people in high flood risk areas?

Brendan McCafferty: The evidence is very clear that, from the day of our launch on 4 April, people who were locked out of the insurance market in the past were able to find

affordable flood insurance policies. The evidence of that is very clear and we had a number of examples of that at the time, including individuals who have been very recently flooded in Cumbria who had previously made a decision that they were unable to find insurance. They were able to find policies costing them £400 or £500 with excesses capped at £250. That evidence is clear. Those people are now able to find their way back into the market.

Mark Hoban: There is also a benefit, Mr Parish, to people who are in high-flood risk areas that have not been flooded. For example, in your own constituency, there is a constituent who has seen their premium fall from £1,200 a month to £935 a month, and in Mr Sunak's constituency from £1,500 down to just under £780. Even those who have not been flooded can see a benefit in a high flood risk area as a consequence of the launch of Flood Re.

Q328 Chair: Are you confident that people are able to access Flood Re, they are getting it at affordable prices and they do not have huge excesses? This is the bit that you are particularly set up to deal with, is it not?

Mark Hoban: Absolutely. What we have seen is that we charge insurers an excess of £250. If they charge their customers a higher excess, we would charge them the same excess. What we have seen across the market is excesses falling to £250 and effectively being capped at that. We have seen an excess benefit come through. As long as customers shop around, they should see a decrease in premiums as well.

Q329 Chair: You made an interesting point about shopping around, because we were down in Somerset taking evidence and there were one or two people there saying they were finding it difficult, even with Flood Re, to start getting insurance. I do not know whether you need to emphasise that a bit more—that they need to shop around.

Brendan McCafferty: There is always more we can do to get the message out regarding shopping around. We continue to do that and put great effort into doing so. You may have noticed at the time of launch we had a considerable media campaign to get that very message out to consumers and we will continue to put that out. If people look at our website, they will see that we launched with 16 insurers on the first day of our launch. We have now doubled that to 34 or 35 insurers and we expect to have 40 insurers by the end of the month. The choice is there for consumers to access, provided we are successful in helping them understand that that is what they need to do.

Q330 Chair: Of those 34 companies at the moment, if I was in a flood risk property that I was finding difficulty in getting insurance for, would they necessarily be interested in insuring my home in any given area? Do they offer insurance for certain parts of the country? How does it work?

Brendan McCafferty: 70% to 80% of people who want to find an insurance quote will go to a price comparison website. We know that. The evidence at the moment is that people who were either locked out or found it extremely hard to find an affordable quote for insurance in the past because they were risk exposed can now get multiple quotes. Around 80% of consumers will find that they are given five or more quotes. 70% will find that they can get 10 or more quotes, all of which will be in that affordable bracket of £500 to £600 with those capped excesses. We are putting measures in place to make sure that,

over time, we are on top of knowing what is going on with consumer pricing. We will share information in due course about that and produce an indices of the experience that people have.

Q331 Chair: Can they contact you directly?

Brendan McCafferty: We are a reinsurance business. Our intention is not to ever have a direct relationship with consumers. We sit in the background, facilitate and enable a market and competition to occur. The evidence is that that is working, as we have just discussed. However, we did recognise the importance of getting a message to consumers that they need to shop around. Therefore, we took that step of taking those measures to get the message out. We will continue to do that for the next year or so, as we go through a year's worth of renewals in the marketplace.

Q332 Chair: If we, as MPs, have constituents coming to our surgeries who are finding it difficult to get insurance, are we able to contact you directly?

Brendan McCafferty: Yes. We would want to have open access with policy makers and we will take an active interest in helping find solutions.

Q333 Chair: That was not a direct answer: you would like to have. Do you have such contact?

Mark Hoban: A number of your colleagues have already written to us about this. While it is not our role to replace insurers and the dialogue between themselves and their customers, it is, from time to time, useful to get a sense of the challenges people face with insurers. That is why, prior to the launch, we did eight roadshows across the country in flood risk areas to understand some of the challenges and get a sense of what the market is like on the ground. We always welcome letters from former colleagues.

Q334 Chair: The main thing is it that it does deliver what it says on the tin, and that is affordable insurance without excessive excesses. Perhaps I have a natural scepticism about whether insurance companies are always going to offer that willingly. Sometimes there may be a need to add a little pressure. You possibly are not going to encourage a hotline to yourselves from MPs but I wonder whether there is not an approach where we could actually get to you relatively easily, rather than writing to the Chairman or the Chief Executive. I do not know whether that is possible and whether you would consider that.

Brendan McCafferty: We would certainly consider that, of course.

Q335 Chair: You are being very careful with your wording here. Did you have a Foreign Office career before this? You may be considering it but are you likely to do it?

Mark Hoban: If your colleagues wanted to write to us directly, that is not a problem at all. What we cannot do, of course, is arrange an insurance deal for your constituents. Having that intelligence on the ground about who might be missing out is helpful to us.

Q336 Chair: What would be useful for us, as MPs, is if we have constituents where they may think and we think that the system is not working properly, we need a process of being able to get to you reasonably succinctly.

Brendan McCafferty: I agree.

Chair: You do. You are going to do something about it.

Brendan McCafferty: We will do something about it. I would add that we put great effort into making sure that all the information that we believe a consumer needs to have in order to access Flood Re benefits is available on our website. It is a great source of reference there. It provides explanation about how it works and the action that is needed. It lists the insurance brands that uses Flood Re and encourages them to take the action of shopping around.

Q337 Chair: You are only a few months in now. How would you judge yourselves and Flood Re so far?

Brendan McCafferty: So far, so good. We remain diligent—

Q338 Chair: Marks out of 10?

Mark Hoban: You should never mark your own homework, Mr Parish.

Chair: I was trying to get you to do that.

Mark Hoban: The anecdotal evidence we have so far that we have shared with the Committee around the reductions in prices and the reductions in excesses demonstrates that, at this stage, Flood Re is having the desired impact. As Brendan said, we are benchmarking insurer pricing. We have a baseline study and we will be looking at that regularly to make sure the benefit of Flood Re is passed on to customers.

Brendan McCafferty: I am encouraged by the fact that consumers continue to display such strong support of our efforts, evidenced by the growth in the number of insurers that are on our panel.

Q339 Angela Smith: Let us see if we can get more of an idea of that mark out of 10. Can I draw attention to my declaration in the Register of Interests? I did visit Whitehouse Construction, which specialises in resilience to floods in terms of the products that they manufacture.

We know that you have a 25-year exit strategy for this product and this mechanism. The Committee on Climate Change is concerned that this scheme will disincentive the measures needed to ensure successful exit—in other words, flood prevention investment by the Government on the one hand, and measures on the part of property owners on the other, to make their homes more flood resilient. What is the industry's view of the Government's approach so far to ensuring that we invest in the flood prevention measures necessary to ensure that we can exit from this programme?

Brendan McCafferty: I am not sure we can speak for the industry. We can speak for ourselves in this regard.

Angela Smith: That is a fair point.

Brendan McCafferty: We have a clear aligned interest with the industry and the Committee on Climate Change to see the measures being taken that are necessary to reduce the cost of flooding, because we interpret the legislation as meaning that when

Flood Re no longer exists, in 2039, people will still be able to find and afford their flood insurance. We want to see the policy steps and initiatives being taken to cause that to happen. That implies that we need to be involved in that and we need to help that process along. There was a very strong convergence between us on that.

Q340 Angela Smith: What are you doing to encourage the Government to invest in the necessary measures?

Brendan McCafferty: So far, in our first transition plan that we published in February, and which will be reviewed in due course, we have sign-posted three areas of activity that we will start to pursue over the coming period of time. First, we will produce our price benchmarking, which will allow us to understand the prospective trend in pricing over time. Secondly, we have said that we will work out what role Flood Re may play in introducing incentives to encourage those right behaviours and responses. Thirdly, we will look at how we may share our data asset that we will accumulate over time, which should be very considerable, and have new information in that regard. It will represent a picture of where the industry sees this risk as being geographical. We will also see the claims connected with that.

Q341 Angela Smith: The latter part of your answer is a little bit clearer, but I am still struggling to see what the ABI is doing and what message it is sending to Government in relation to the importance of the Government taking the measures necessary to ensure that you do not have to continue with this programme in 25 years' time.

Brendan McCafferty: The insurance industry continues to be at the forefront of making the case that continued and increasing investment in flood defence is needed. Flood Re would support that. From our point of view, we need to make sure that we put that in the context of the effect on prices over the period of transition we are charged with managing.

Q342 Angela Smith: Do you think the Government are doing enough at the moment?

Mark Hoban: The Government have set out in their spending review about £1.2 billion over the lifetime of this Parliament and the next Parliament. We welcome that. The challenge that Flood Re brings to this process is, as Brendan said, that we will have a comprehensive map of flood risk and our contribution to working out where that money will be spent will be, "These are the areas where we believe there are the most homes at risk". We would like to see money spent in that area because if you spend money there and reduce the risk of flooding, that is likely to reduce the overall cost of flooding, which will ensure there will be affordable low and sustainable prices once Flood Re comes to the end of its time.

Q343 Angela Smith: In terms of ensuring that Flood Re informs the Government about what they need to do, are you making use of the latest Met Office and Environment Agency data, and keeping yourselves informed of what the Committee on Climate Change is saying in terms of the very important nature of the message that we need to send to Government? It is not enough to say—and forgive me, Mark, you were once a member of this Government—that the Government have put so much in its spending plans; surely they have to be continually reviewed and the ABI has an interest in making sure that it keeps sending that message back.

Brendan McCafferty: We have a stated strategy of working very closely with the full array of agencies, academics and the industry, in order to properly understand those considerations and make sure they are factored in to our thinking and our view about what is necessary to keep prices affordable. We will take account of all those things and we will comment on the measures that we think are appropriate in order to bring that about.

Mark Hoban: Flood risk management is only one aspect of the measures we have taken to reduce the overall cost of flooding. In our transition plan, which was published in February, we identified three areas of activity: first, flood risk management to try to reduce the risk of flooding; secondly, betterment and resilience, so where there is a risk of flooding, properties are more resilient to that risk; and thirdly, around the cost of flooding once a property is damaged. There is a range of areas where we feel we have contributions to make and we should not look at one area in isolation.

Q344 Angela Smith: I started my question by making that clear, but I was focusing initially on the Government's role on this in making sure that we can exit from this scheme in 25 years' time. The second aspect, indeed, is resilience. Is the industry and the ABI prepared to recommend insurance products under Flood Re that will require homeowners to build flood resilience measures into their properties?

Mark Hoban: We are not answering for the ABI.

Q345 Angela Smith: Sorry, for Flood Re. I do apologise.

Mark Hoban: We are at an early stage of our development. We need to engage with industry and understand what measures around resilience work, what is affordable and what will encourage homeowners to make their homes more resilient. We have been through a period where homeowners have seen their premiums go up and they have seen excesses rise, yet that has not triggered homeowners to invest in resilience measures themselves. There is a lot of work to be done, not just on the effect of individual measures but also on how we work with insurers and homeowners to encourage them to make their homes more resilient.

Q346 Angela Smith: Whatever the measures necessary prove to be, are you in principle in favour of rewarding policyholders for taking those measures and building them into their homes?

Brendan McCafferty: Providing that the evidence supports the case that that is the right thing to do and that it would represent value for money, remembering that we are a public body, or will be. We have to be careful to make sure that any incentive we provide, at least with a financial consequence to us, has merit, but yes, we are.

Q347 Chair: Surely, your role is as much to advise the insurers as it is to have a direct role. What are you doing to talk to insurers so that they are incentivising, with their policyholders, flood resilient measures? What talks are you having with insurance companies?

Brendan McCafferty: We will be working very closely with insurers to make sure that we are using, again, our data to understand what the best practices are, as Mark has said, in terms of reducing the cost of flooding events from an insurance perspective. We will share those best practices as we are able to, within the constraints of competition law. Also, we will work with them to understand the effectiveness of measures that could be

taken. As we have said in our transition plan, we will consider what that might mean for our own stance on incentives for insurers.

Q348 Chair: Even in terms of simple things, like putting electric sockets out of a potential flooded area, so that if you did flood you would have those sockets higher—not everybody wants them up higher because they do not look particularly sightly—are you bearing down on things as practical as that?

Brendan McCafferty: This whole topic is an immensely practical thing. That is where it has to take us to. I echo Mark's comments that part of this has to be about changing the attitudes of consumers. It is not just insurers who can make this difference; consumers need to see that as an acceptable thing to do. We need to put it in the context of the consumer's attitude.

Q349 Angela Smith: As part of that, changing attitudes may involve a mechanism that replaces the like-for-like principle. One of the issues may be around, when someone's property is unfortunately flooded, them being allowed, under the scheme, to not do like-for-like, but better because of the need for resilience.

Brendan McCafferty: Yes, we are talking about betterment. There is a change in attitudes to that occurring in the industry. I am sure my colleagues will comment on that later. Again, we will look at what the evidence suggests is the right thing to do. We will consider our scope for incentives in that context.

Q350 Rishi Sunak: Thank you for being here. When someone buys a house, do you know if there is any legal requirement for the fact that they may be using Flood Re in their insurance policy? Would that be disclosed? Does it need to be disclosed?

Brendan McCafferty: Currently, the Council of Mortgage Lenders' requirements and the Law Society guidance requires the collection and disclosure of the occurrence of a flood claim. People are asked questions about whether they have been flooded in a particular period of time and whether they have made an insurance claim. I am not aware of any suggestion that that guidance would be changed, given the launch of Flood Re, to ask an additional question about a policy being sent to Flood Re.

Mark Hoban: It is a very interesting question. When we did our roadshows earlier this year, one of the comments that came back from people who had been flooded or at risk of flooding was that flood or risk of flooding created a blight over their property in terms of being able to sell it. A lot of people in high-flood risk areas thought that the existence of Flood Re and therefore the possibility that some will get affordable flood cover with low excess actually gave them the opportunity to sell their home when perhaps they had not had that opportunity before.

Q351 Rishi Sunak: That may well be right. Given it is a time-limited scheme it is about making sure that people are aware when they are buying properties. I take your point it may have an impact on the value. They may be benefiting from an insurance scheme that is not going to be there forever, so people should have full awareness of that.

The second, unrelated point is that we live in this world of open data and better data, and Defra is trying to do a better job of getting its data out into the public domain. Is there data that, if the insurance industry could get its hand on it, would improve its ability to offer flood

insurance, either at your level or the retail level? Are there things that, if we knew about them—a kind of mapping or geographical information—would help us target policies and mean that we could say, “You guys are fine” and reduce the number of people who would be impacted by lack of coverage?

Mark Hoban: In a sense, it goes to the heart of why Flood Re was necessary in the first place. As insurers improve the quality of their mapping and understanding of flood risk, what you have seen is their being able to price more accurately based on risk. That has benefitted those people in low flood risk properties but also it has driven up premiums and excesses for those in high-flood risk properties. The data have already been used. From our perspective, what Flood Re will bring is access to a source of data that will be the most comprehensive risk map of flood risk based on properties ceded to us. It is our view that we should share that data as far as it is commercially practical with local authorities, the Environment Agency, Government and others to help inform the decisions people make about flood management—for example, where defences should be and where we should perhaps have more resilient communities. We see our database as a key asset in trying to tackle the problem in the long term.

Q352 Chair: One of the problems people have had, although the mapping is getting more accurate, is that if you are in an overall flood area, very often you are lumped into an area where you are prone to flooding, even if your house or property may be a little bit higher than the surrounding ones so you probably do not get flooded. At the moment, I do not know whether it is getting better and what influence you have over it being much more related to your individual property than it has been.

Mark Hoban: Certainly conversations we have had with insurers would indicate that a number have made quite significant investments in their mapping and are able to price on a property-by-property basis, rather than by postcode sector. They will know that number 20 is on a side of a hill but number 21 is at the bottom of the hill by the stream. That is part of the process that has meant that risk is priced more accurately and, perhaps, unwound some of the cross-subsidy that has previously kept premiums lower for high flood risk properties.

Brendan McCafferty: Even though we possess probably the best flood maps—certainly amongst the best—in the world, even recent events reveal the fact that flood maps are still deficient. Therefore, the insurer’s ability to know where the floods are ahead of time is limited still. There is still a considerable journey to go on before we can say that those flood maps are accurate and reliable in every case.

Q353 Chair: My farm is in a flood plain. These are fields, not houses. When we have a major flood, you will find that some fields will flood and others will not because of a metre of difference in height. Yet as far as the map is concerned, it is all within the flood zone. That is where we have a problem with some properties sometimes.

Brendan McCafferty: When we translate that into domestic properties, we are talking about the height of doorsteps and things like that, which are considerably granular.

Q354 Chair: Are you beginning to drill down to that level?

Brendan McCafferty: Yes. That is where things are on a journey towards. That will take some considerable time.

Q355 Ms Ritchie: Good afternoon, gentlemen. There are concerns that should an exceptionally large flooding event occur, such as Hurricane Katrina in the United States, there would be insufficient reinsurance cover to fund all insurance claims. In that context, will the funding mechanism for Flood Re provide adequate cover for severe flood events of the future?

Brendan McCafferty: If we start with the way in which Flood Re is set up, we are able to cope with claims from insurance companies up to £2.1 billion in any year. I can try to put that into some kind of context for you: if you look to the most recent storms over the last winter, which generated residential property claims of about £500 million—about 9,500 claims—Flood Re would expect to see about a third of those claims. For us, that would have meant a gross cost of £150 million. There you have the relativity between the £150 million and the £2.1 billion. In fact, half of that £150 million cost would be met by our own reinsurance provision. Our profit and loss effect would be £75 million. If we look at 2007's weather events, which were certainly the worst in the last 10 years, the gross cost of the residential property claims was £973 million. Again, Flood Re would have expected to have seen about a third of those claims, which would have meant a gross claim of £360 million and a third to a half of those claims would have been met through our own reinsurance. Hopefully you can see from that that the £2.1 billion capacity that we have to meet claims, put in the context of those two events, demonstrates that we have a considerable amount of headroom. We are engineered to be able to meet claims that, on a national level, would be a one-in-200 national event and beyond.

Q356 Ms Ritchie: Just seeking further clarification, how will Flood Re assess whether new areas are becoming at high risk of flooding as a result of the increased likelihood of extreme weather, climate change, El Nino or whatever you want to call it?

Brendan McCafferty: We are beginning to take steps now, which we have launched, to make sure that we are absolutely at the forefront of understanding, be it from the academic community and other places, what the analysis, thinking and hypotheses are about what will happen. We will make sure that is factored into our modelling and our assessment of what that might mean in terms of our insurance risk. We will include that in our thinking in terms of looking at the level of risk that we need to be able to bear at any point in time.

Mark Hoban: As well as that top-down approach, as insurers' understanding of changing risk works its way through their own processes, we will see where they are ceding risks from. Maybe there is an area from where they do not see cede risks to us. If their understanding of flood risk changes, so they now see it as high-risk, we will see those properties coming on our books as well. We will see it from that macro perspective but also that micro perspective as well.

Q357 Ms Ritchie: When you are looking, perhaps, at Government perspective, what mechanism is in place for Defra, working in co-operation with yourselves and the Treasury, to assess if Flood Re has sufficient funding?

Brendan McCafferty: We need to remember, first, that Flood Re is a privately owned and operated insurance vehicle. We will use the mechanisms that that suggests. That means

that we will use our flood modelling, we will be close to the industry and we will take all the measures that any commercial reinsurer would take to capture that. We will show, appropriately, the Treasury and Defra the information they need so that, from a policy perspective, they can know that we are able to meet that obligation.

Q358 Ms Ritchie: We know you are in very early days. Have you been sharing information with Defra and Flood Re already?

Brendan McCafferty: In relation to how we have gone about demonstrating that we can meet the obligations that are given to us in the legislation, yes.

Q359 Ms Ritchie: Is Flood Re resilient enough to handle flooding damage that exceeds the damage we saw over the Christmas period of 2015 and early 2016?

Brendan McCafferty: Absolutely. The resilience of £2.1 billion of cover is in disproportionate terms to that event in 2015-16.

Q360 Ms Ritchie: I wrote to you, Mr McCafferty, to find out if Flood Re extended to Northern Ireland, where there are certain levels of flooding and certain areas where there are flood plains. They have been building in that particular area. Just to clarify, you do extend to Northern Ireland.

Brendan McCafferty: We do extend to Northern Ireland, subject to the exclusion that we do not cover properties built after 1 January 2009.

Q361 Ms Ritchie: Have you been in direct discussion with the Department of Finance and the Department of Agriculture, Environment and Rural Affairs in Northern Ireland about this scheme?

Brendan McCafferty: Not yet, no. We have plans to engage with the devolved administrations in the months to come at a more detailed level.

Mark Hoban: We were keen to get the May elections out of the way and then talk to the Ministers in the various devolved Administrations.

Q362 Ms Ritchie: They are now two months out of the way. We would imagine that you would be doing so.

Brendan McCafferty: Absolutely.

Mark Hoban: Absolutely.

Q363 Rishi Sunak: I understand that this is the first time in the world anything like this has been done. Have you had people from other countries in policy-making positions come to you at all to learn more and see what is going on? I know it is early days.

Brendan McCafferty: We have indeed, and that continues. We have had particularly close conversations with Canadians. We have helped them. I have been over to Canada to help them understand what their policy reaction might be because they are suffering similar problems. We have also spoken to the Australians. We are talking to the Netherlands. I have representatives from the People's Republic of China coming to see us later this week. Absolutely, we continue in London to be seen as a centre of leadership

and thought around topics like this. People do make their way to us. We are, as we can, sharing information with them about what we are doing.

Q364 Chair: It is interesting that you talk about the Netherlands, because they have not had a history of individual properties being protected by insurance because it is state protection because of 16% of the country flooding. I want to drill down exactly how you are certain you have enough funds. Basically, you have a levy on everybody's insurance policy to pay into a fund. My simplistic view was I thought it had to run for several years without a major claim coming in in order to make sure you have enough funds. I also want to check what you said just now; it looks like you are insuring your risk somehow or other. I did not quite understand quite what you were doing. Is it clever? Will it work? Is it too clever for its own good? These things have been done before.

Brendan McCafferty: Just to pivot between the two points, we are different to a lot of the international schemes, although we share some of the same characteristics. Mr Chairman, yes, we do buy reinsurance from the global reinsurance market. That is a feature of what we do. It is the thing that enables us to, with £180 million income, stretch to £2.1 billion reinsurance cover. I am sure we will see in the future claims being paid by the reinsurance market on our behalf. That is what insurers do and that is what we will do as well.

Q365 Chair: When you sell this risk or buy this cover, surely it is very much in the hands of those who sold you the cover if there was a major claim that they themselves could have enough funds to cover. I am not entirely convinced by this. If you have an absolutely major flood, I am not certain that the private sector would be able to fund it and I am quite certain that the Government would have to come in as the insurer of last resort. I am not entirely convinced. You have to convince me.

Mark Hoban: I will try to help convince you, Mr Parish. It is a question that the Board went through in some detail. We will bear a proportion of the losses. We are exposed to £175 million worth of losses every year before we take the full benefit out of reinsurance cover. We went through a procurement process to acquire our reinsurance cover. We limit our exposure to any one insurer and we also expect a good credit rating for each of those insurers to try to minimise that risk.

Q366 Chair: Do you spread your risk across a number of companies?

Mark Hoban: Yes.

Brendan McCafferty: We have over 40. We have a limit on how much capacity we will take from any individual reinsurer.

Q367 Chair: Am I right in saying that the more years it goes on where you do not have a major claim is better, or is that irrelevant?

Mark Hoban: You should pray, Mr Parish, for dry weather for the next few years.

Q368 Chair: Unless we have a drought, where we may need to pray for rain.

Mark Hoban: The way the model works is we levy £180 million a year from the insurers who also get premium income for every risk they pass to us. Clearly, the surplus we make every year helps us build up our capital reserves. Assuming the weather is reasonable in

the next three or four years that will enable us to build up those reserves. In the event of our reserves being insufficient to meet losses, we also have the ability to levy a second levy on the insurance industry—levy 2, as it is explained. We get £180 million per year plus the ability to have levy 2 to make up any shortfalls.

Q369 Chair: Naturally, you would have to be able to justify making another claim.

Mark Hoban: Absolutely.

Brendan McCafferty: We do to an extent. The legislation says that it is at the entire discretion of the Board of Directors at Flood Re.

Q370 Chair: I see. The insurance companies might have something to say if they thought you were levying it more than you needed to. I am sure you would not do that.

Brendan McCafferty: No.

Q371 Rishi Sunak: Is there a meaningful float income? How early do you get the premiums from all the policies? How are you managing the float? Are there any guidelines about how you manage it, or is it outsourced?

Mark Hoban: In terms of the levy, we build that quarterly in advance. We get our capital in. There is an obligation to pay that. That is one of the reasons why the levy is set out in the statute in the Water Act. That revenue flow comes in and we get the premiums as policies are ceded to us by the insurers to supplement that.

Brendan McCafferty: We invest in cash and gilts and use the Government debt office in order to put most of our funds on deposit. We are extremely cautious and safe about it.

Q372 Chair: You are not speculating at great risk, then.

Brendan McCafferty: Not at all.

Chair: Time will tell on that one.

Q373 Angela Smith: Hopefully you do not have to invoke it but is there any limit on levy 2, in terms of what you can raise?

Brendan McCafferty: It is unlimited.

Q374 Angela Smith: The need for negotiation and trust on both sides is quite strong.

Brendan McCafferty: Absolutely. It was a very big commitment for the industry to make to allow that to be put in place.

Q375 Chair: The argument now is even if the weather is reasonably good, we will still get a major flood either every other year or every year. We are getting a lot of flash flooding in certain areas. Have you have factored that in?

Brendan McCafferty: Yes, we have. We believe that is reflected in our modelling, which in turn informs our view of what a normal year's losses may look like. That could mean we will pay £60 million to £90 million of claims every year in a normal non-event year.

Q376 Chair: In a utopian world, where we do not have any major floods for a while, you will be paying money back eventually, will you?

Mark Hoban: The way it works, Mr Parish, is that every five years there is a review with the Secretary of State where we discuss the levy and the tariff. That is the point where those conversations will be had.

Q377 David Simpson: In relation to one of the comments you made at the very start, Mark, in relation to the premium prices of the money, maybe I am quoting you wrong but you said there was one example where it was £1,200 but it went down to £900 per month.

Mark Hoban: Per year.

Q378 David Simpson: It would be very expensive insurance if it was per month. I just wanted to clarify that position. The other thing is that you made the point—you did not say it, but the Chairman said it—that there is not going to be a hotline to you guys in relation to policy purchasers or holders. Is it then up to the insurance companies and the buyer of the policy to have full transparency of the policy itself in the small print? We always hear the comment from people who claim their insurance that the small print says something different. How do we ensure open transparency in all of this?

Brendan McCafferty: To be clear, we do not have a policy with the consumer. The consumer buy their policy and it remains the same. They have the contract of insurance with the primary insurer.

Q379 David Simpson: Is it up to an insurance company, then, to be open with them and the purchaser to dig deep enough to know that if there is a flood it comes to the small print: “I am sorry, you are not covered”?

Brendan McCafferty: It is. We always say in our advice that consumers should take a very active interest in ensuring that the policy they choose is appropriate for their needs.

Q380 David Simpson: A question was touched on before in relation to the transition period. Can you clarify for us how you can ensure the transition will be smooth?

Mark Hoban: In February, we published our first transition plan. We will revisit that again over the next two or three years. We will set out the actions we believe should be taken to reduce the cost of flooding; that is whether it is by Government, by the Environment Agency, devolved Administrations, insurers or householders. What we should see over time is that the cost of insurance remains relatively static for householders but the cost of flooding itself comes down. Therefore, the levy comes down. Our goal is that, in the long term, we should have sustainable and affordable prices without the existence of this subsidy by the industry.

Q381 David Simpson: Why are insurance companies enthusiastic about this scheme with your involvement because, prior to this, we have heard the message in the Chamber that people cannot get insurance? Brendan, you have said that there were 17 insurance companies on board; you have now doubled that. Why is that? Are you making it attractive or is it more attractive to them?

Brendan McCafferty: I believe it is because the industry took the issue so seriously. We are talking about a significant number of customers who it was clear were experiencing a market failure. The industry took its responsibilities very seriously indeed. I know that my colleagues will comment later, but my understanding is that it was the industry that took the concept of Flood Re to Government.

Q382 Chair: I would be a bit more cynical than that. Though insurance companies are supposed to be insuring risk, they are risk-averse. Therefore, they are now farming out their risk to Flood Re. Is that not exactly what they are doing?

Brendan McCafferty: Yes, they are but they are also, at the same time, bearing the cost of £180 million annual levy, which in the context—

Q383 Chair: No, they are not; the consumers do. The consumers pay that.

Brendan McCafferty: We are in a market where prices have continued to reduce year on year. Their ability to recover that levy is questionable.

Q384 Chair: On the question that David asked, could I put it in a slightly different way? If an insurance company has been accepted by you into Flood Re and then there is a claim by an individual, surely when you accept these companies for the Flood Re process they must also have to submit their terms and conditions of how they are going to offer the insurance to the individual. If they were not fulfilling that, surely you have a role to say to the insurance company, “When we accepted you into the Flood Re policy, you said you would provide insurance in a certain way”. If they were not doing that, what powers, if any, do you have over the individual insurance company?

Brendan McCafferty: We have contracts in place with each of the insurance companies concerned where we are able to go and check that the claims that they are making to us reflect the position they are taking with their customers. It is for the insurance company to decide whether or not to pay a claim. Flood Re does not have a direct role in doing that.

Mark Hoban: If a customer is unhappy, they can go to the Financial Ombudsman Service to make a complaint once they exhaust the process with their insurer. The existing relationship between insurer and their customer remains unaffected by the existence of Flood Re.

Q385 Chair: Do you not have a watchdog type role at all, then? You are just an insurance broker.

Brendan McCafferty: Our responsibility is to ensure that any particular insurer is not trying to gain an advantage in seeking to settle claims that are higher level for Flood Re claims than they would for any policy or claim that was not sent to Flood Re. We take measures to ensure that that is the case. Beyond that, no.

Q386 Chair: Therefore the consumer has to be just as careful, if not more careful, when they are taking out a policy with the individual company. They cannot come back to you in any shape or form.

Brendan McCafferty: Correct.

Chair: That is interesting. People need to be very much aware of that.

Q387 Dr Monaghan: Good afternoon. I am sure you know that Flood Re does not extend to businesses. This Committee has heard from the Government that they believe that it should not because there is no systemic market failure in relation to the insurance of business premises. Equally, this Committee has heard from witnesses that businesses are having difficulty accessing insurance in certain areas. How can affordable insurance be provided to businesses in risk areas?

Brendan McCafferty: This is a question for my colleagues in the industry rather than for Flood Re. It is not something that is within our scope. It is clear that the question of affordability for businesses is rather more difficult to address than one for households. The information around what the extent of the problem is ought to be the right starting point. That should include something around affordability. I know that the industry and the British Insurance Brokers' Association are taking some steps to try to resolve what is accepted to be some degree of a problem, especially for small businesses.

Q388 Dr Monaghan: You have said already that Flood Re has significant headroom in this capacity: £2.15 billion relative to what you expected to have to pay in any given year. Does that not create an opportunity to extend Flood Re to the business community in risk areas given that there is, clearly, a systemic market failure?

Brendan McCafferty: I do not believe the evidence is there to make the case that there is a systemic market failure. We are concentrating on making sure that we are successful in implementing the scheme that was agreed by Parliament, which has the scope of domestic properties only.

Q389 Dr Monaghan: Would it not be prudent to develop an economy, and for you to contribute to that, by extending the scope of Flood Re to cover businesses also?

Mark Hoban: The challenge would be for the subsidy—the levy—that is being charged by the insurance industry. It is there to subsidise cover to domestic properties and there is an element of cross-subsidisation there between householders if the levy is passed back to householders. There always had that element, historically, of cross-subsidisation. If you set up a scheme for businesses, who would provide that subsidy? It would have to be other businesses, Mr Chairman. You cannot simply extend the Flood Re scheme using levy that is there for subsidising the household industry.

Q390 Dr Monaghan: No, but the scheme could be adapted in some way. The crucial aspect, as I am sure you will agree, is that businesses do have to have access to affordable insurance. If they cannot do that, it is a critical issue for those businesses concerned. We are hearing, as a Committee, that that is an issue. It is an issue that does not appear to be getting addressed. I accept your point that it is probably for the next panel to be talking about that, but given that you gentlemen both have a degree of expertise in relation to the development of Flood Re and the provision of affordable insurance to households, what are your ideas about how that could be extended into the business community so that outside of Flood Re, perhaps, affordable insurance is made available?

Brendan McCafferty: We have not been asked to do any work or produce any thinking around an answer to that question, so it would be inappropriate to suggest any level of detailed response. Our scheme, and the thing that we have built now, is engineered to deal with the scope that we were given, and only that scope. Should the question arise in the

future, it would raise all sorts of questions and issues that would need to be worked through. That would be considerably challenging.

Mark Hoban: It has taken seven years to get to this point for Flood Re, and it would be good to see if the BIBA scheme answers this problem. It would be better to get something up and running and working quickly. This Flood Re scheme has been the product of quite a long discussion between Government and the industry. There has been a long process of implementation by us. It is not a quick and easy solution.

Q391 Dr Monaghan: Clearly not. Would you be in favour of Defra undertaking a full analysis of the insurance market in relation to businesses, to see if there is scope for an additional complementary scheme that could be implemented?

Brendan McCafferty: Any light that can be shed upon the extent of this problem would be helpful.

Q392 Dr Monaghan: Would you be in favour of Defra doing a full market analysis?

Brendan McCafferty: It is not for me to say who the right organisation might be to do such a thing.

Mark Hoban: It is a matter for Government and industry to resolve. If Defra were to do this, that is their choice.

Q393 Dr Monaghan: Both of you are clearly saying that an extension of Flood Re to cover businesses would not be appropriate and it is not something that you would like to see take place?

Brendan McCafferty: The evidence is not there today to suggest that we would be an appropriate solution.

Mark Hoban: Exactly.

Q394 Chair: We had a lady here from Cumbria who ran a guesthouse. She was having trouble getting insurance. It is quite interesting to know when a house is a domestic property and when it becomes a business. How do you analyse that? How do you decide that?

Brendan McCafferty: We have some extremely clear and relatively simple criteria that we look for to test that any policy is within scope that is sent to us by an insurer. There are three things. First, a property has to be built before 1 January 2009; secondly, it has to have a council tax band; it has to be the principal residence or at least used for the occupation of its owner; it needs to have an insurance policy in the name of an individual. If the property meets those conditions then it is eligible for Flood Re.

Q395 Chair: The lady running a guesthouse, who actually lives in the guesthouse and is council-tax-banded, theoretically should be able to get flood insurance through Flood Re?

Brendan McCafferty: From our point of view, we would accept a policy on that basis. There is an additional question for that person, though, which is: can they get a policy from an insurance company that recognises the need for a domestic policy as being appropriate to their circumstances? She would be under an obligation to disclose to the insurance company that she runs a guesthouse.

Q396 Chair: I want to ask a question now about these properties that were built after 2009. Do we just wash our hands of those properties? How do they get any insurance? It may or may not be the fault of those individuals who are living there that they were granted permission in the wrong places. What do we do about it? Are they just out to sea?

Mark Hoban: Mr Parish, the scheme was agreed between the Government and the industry to have this cut-off point, the sense being that homes built after that point are built to a higher degree of flood resilience than homes built prior to that period. They should not have a problem finding affordable flood insurance. It is also a challenge, if you move that date to, say, 2014, of whether we creating the wrong sort of incentives for developers who feel they can pass the risk on to the homeowner and insurance industry? This is something that the Environment Audit Committee has looked at as well. It is a system of the Environment Agency offering guidance to councils. The view was that in the vast majority of cases that guidance was being followed. There should be a lower flood risk and higher degree of resilience for homes built after 2009.

Q397 Chair: Are you getting many people with homes built after 2009 contacting you?

Brendan McCafferty: No, we are not.

Q398 Chair: Do you not see it as a major problem?

Mark Hoban: No. The roadshows that we did, the meetings that we have had subsequently and the consumer engagement that Brendan has done quite a lot of have not identified this as a huge issue.

Q399 Chair: Do you believe that the majority of those properties are getting insurance, or are they not insuring?

Brendan McCafferty: We expect that they can find insurance, indeed. One would expect that the flood maps that the insurers use would capture the fact that those areas are protected in the nature of the development. The insurers would know that. It would be reflected on the Environment Agency maps.

Q400 Ms Ritchie: It has been my experience that councils have granted planning approval for developments in flood risk areas post 2009. Through no fault of their own, homeowners bought such properties. What do they do if there is a high level of flooding in that area and there is severe inundation of water into their properties that causes destruction of their furniture or whatever artefacts they may have? What can they do?

Brendan McCafferty: In terms of finding an insurance solution, we would recommend that those individuals seek the help of a broker. The British Insurance Brokers' Association hold a list where they can find a local broker. Secondly, they should look at measures that they can take themselves to protect their property.

Q401 Ms Ritchie: Do you not think that Flood Re should be asking the Government to review this particular area and suggesting that Flood Re has an input in this particular regard?

Mark Hoban: In what sense?

Ms Ritchie: To be able to help.

Mark Hoban: We have not seen evidence that there is a problem with people finding insurance. We believe where homes are built on high flood risk areas, as part of the planning process, there should be additional resilience built in. Those protections should mean they are able to find insurance. We have not seen any evidence coming back to us, certainly, that there is an issue in that area.

Q402 Ms Ritchie: Is that not more because you do not offer that level of reinsurance post 2009?

Mark Hoban: No. We have done quite a lot of engagement. Certainly, the events that we have done would have identified if there was an issue. To be candid, going back to the questions about SMEs, in a number of the events we held, people did raise issues about SME insurance. For people in high flood risk areas, if they had a home in a high flood risk area built before 2009, people would say, “I do not want to see any more development encouraged in high flood risk areas because it might make the problem worse”. There is a risk, by extending the scheme to newer properties, that you create some sort of incentive in the development system to build more homes in high flood risk areas, which has a negative impact on homes that are already built.

Brendan McCafferty: I have been struck by the number of people who have asked about this. I have expected them to query why it was done. Actually, they want to support it. They want to say: “We do not want people to suffer the misery that we have had. Doing what you have done from a policy perspective does encourage the right development measures to be taken. We support what you have done.” That is the opinion of people affected by flooding.

Q403 Angela Smith: Conversely, the insurance market is a really good way of assessing risk. Do you think that the views of the insurance industry ought to be sought when proposals are put forward to planning committees for building in high-risk areas? Just as the Environment Agency is a statutory consultee, then perhaps the insurance industry’s views also ought to be considered. Building homes in places where insurance is going to be hard to get, except at a very high price, does not seem a very sensible thing to do.

Mark Hoban: If you think about the number of insurers that participate in our scheme, if a local authority was to write to each one, it would be quite burdensome. There is a role for the insurance industry to play, broadly, in ensuring there is a proper dialogue between planners and the Environment Agency and there is thinking done about the impact of new development and the consequential impact on older homes that could increase the risk of flooding. Consulting the insurance industry on a development-by-development basis might be quite time-consuming.

Angela Smith: I know you cannot speak for the ABI but maybe there is a role for the representative body of the insurance industry to either have that dialogue or have an input in one way or another.

Chair: There might well be a role for the local authority to highlight the attitude of the Environment Agency and also the potential insurance liability if property were built there. Perhaps that is something we can raise through our report with DCLG.

Q404 Ms Ritchie: Flood Re, as you well know, is industry owned but was given statutory underpinning by the Water Act 2014, therefore making yourselves directly accountable to Parliament for your achievement of policy objectives. In that regard, how can you reassure customers and Parliament that the funds raised by Flood Re are accounted for properly?

Mark Hoban: There are a range of measures that we are taking to do that. First of all, Flood Re is subject to audit, not just by our own auditors but by the NAO for value-for-money grounds. We are accountable not just to this Committee but also to the Public Accounts Committee. We have to follow the Government's value-for-money rules. There are certain processes we have gone through to demonstrate our adherence to those rules.

Q405 Ms Ritchie: Is that due diligence?

Mark Hoban: No, we have applied the OJEU process for public procurement to the section of the people to whom we outsource business operations. We also use it for our reinsurance programme, which is a radical departure from the way in which reinsurance normally works. We try to make sure there are processes in place throughout the business to demonstrate that public money is being spent properly.

Q406 Ms Ritchie: Are there any other measures in place to ensure that insurance companies are not setting unnecessarily high excesses through Flood Re?

Mark Hoban: On the excess point, we will charge insurers an excess of £250, which they pass on to their customers. If they were charged an excess of £1,000, we would charge them an excess of £1,000. There is no incentive on them to game the system.

Q407 Ms Ritchie: Without the existence of Flood Re, how many households do you estimate would be unable to access affordable insurance?

Brendan McCafferty: It is a number that we were never able to establish with any certainty when we looked at the extent of the problem. We know that that problem was growing.

Ms Ritchie: Come off it. I am sure that you have done your assessments—

Brendan McCafferty: Several thousand properties but it is very difficult to be precise about that.

Q408 Ms Ritchie: Do you honestly think, Mr McCafferty, that we as a Committee believe that? We assume that you have carried your assessments in order to have your financial projections.

Brendan McCafferty: We believe that when Flood Re reaches maturity there will be about 350,000 households benefiting from our existence. That is the number we reasonably expect to get to. What proportion of those were locked out of the insurance market before we launched is an unknown quantity. It is worth saying that it could be considerably more than that who benefit eventually.

Q409 Chair: You think it is 350,000 eventually. What are you starting off with? What do you believe it will be in your first year?

Brendan McCafferty: The trajectory to get to 350,000 would be over about three years.

Q410 Chair: What are you expecting this year?

Brendan McCafferty: We are not in a position to know that because those are the decisions that have been made by the insurance companies. It is up to them to decide.

Q411 Chair: You cannot work out your funding, whether you have enough money or anything. You do not have any idea. Now, come on. You must have some idea.

Mark Hoban: Mr Parish, the situation is that it is the insurers who decide which properties to cede to us. We know we have the levy of £180 million a year. The insurers need to decide which properties they pass to us. We referred earlier on to some of the examples of the benefit we are seeing from Flood Re quotes. To go back to Ms Ritchie's question about people who could not insure, there is another question about how many people found it difficult to afford insurance. A house had been flooded in Brampton in Cumbria in 2009. The homeowner there was being charged a premium of £5,816 a year and an excess of £25,000. It may not be that someone was excluded from insurance but had to make quite big financial sacrifices. That property is now paying an excess of £250 and a premium of £810. It is not just those who could not and therefore did not buy, but those who had to sacrifice a huge amount to be able to get the reassurance that most of us pay relatively small sums for.

Q412 Ms Ritchie: In order to reassess those particular levies on an annual basis, do you intend to be meeting with the Met Office and others involved about projecting potential weather patterns over the next year or two years in order to help with the assessment?

Brendan McCafferty: Yes, absolutely. That is a fundamental part of what our modelling is there to do.

Q413 Ms Ritchie: When will that take place?

Brendan McCafferty: We do it all the time. We are at the stage now of wanting to reach out to agencies like the Met Office and the Environment Agency to deepen those relationships and conversations. We already have a very, very good view, from an actuarial and risk perspective, about the impact of weather events, their frequency and the severity of events in general.

Q414 Chair: Surely, with that, you will be projecting numbers.

Brendan McCafferty: We have a very vast range. I go back to the point I made earlier on—

Ms Ritchie: Could you define vast range?

Chair: Where do you start and where do you finish?

Brendan McCafferty: Our midpoint is 350,000. All things are possible beyond that. It will depend, not least on the commercial impact that any events have on insurers, too. They may well want to send more risk to us if they perceive that volatility is increasing. Equally, if they believe that weather patterns are not as bad as we may fear, they may hold on to more of that risk.

Mark Hoban: If you think about this winter's flood and talk to some of the insurers, they see the volatility in claims that affect their profitability. They see a way of reducing that volatility by transferring business to us. Their appetite to use Flood Re will increase. It is their underwriting positions that will determine how much business we get. It is determined by a whole range of factors, most of which are outside our control.

Q415 Chair: I have a simplistic question that may not apply to you. Will you prepare accounts, will they be audited and will they be presented to Parliament? Do you go through that process?

Mark Hoban: Absolutely. We are in the process of preparing our accounts for the year to 31 March 2016. They will be laid before Parliament. We will send you a copy as well.

Chair: I very much look forward to it. Perhaps we will bring you in again and ask you some new questions.

Q416 Dr Monaghan: If Flood Re makes a profit, where does that go?

Mark Hoban: Going back to the conversation we had earlier on about the losses that we potentially bear on claims, the profit that we make builds up our reserves so it increases our ability to bear those losses without having to resort to levy 2. At the five-year review, we would look at our projections for future losses and think about prices and the levy in that context. Our reserves would help, for example, if we have had a good year, to reduce the levy and prices and, if we have had a bad year, we may have to increase the levy and prices. The profit we make helps to create a more financially resilient organisation.

Q417 Dr Monaghan: Building up reserves and establishing a profit are different things, are they not? Are you saying that Flood Re will never make a profit that is distributed to anybody? Are all of the surpluses generated going to reserves?

Brendan McCafferty: Yes. We do not have a profit distribution mechanism at all, with one slight caveat, which is if we were to call a second levy, there are mechanisms that that could be refunded to the contributing insurers over time. There are very, very strict rules about what circumstances need to prevail before that would happen. At the termination of the scheme, those remaining funds that are left on the balance sheet when the enterprise closes down in 2039 would be repatriated to the Secretary of State.

Mark Hoban: To be very clear, there is no mechanism for us to declare a dividend and pay it to insurers, if that is the concern that you have, other than the levy 2 example that Brendan quoted.

Q418 Dr Monaghan: From what you are saying, I take it you will confirm that as the years pass and hopefully you do build up that reserve, if that reserve is getting significant you would look at the levy and adjust it to manage the situation. What would you imagine that levy or that level of reserve to be when you would take action to address the levy situation?

Brendan McCafferty: I am afraid it will depend upon the degree of risk we are carrying on the balance sheet at that point in time. We are also conventionally regulated by the Bank of England Prudential Regulation Authority. We would need to look at the rules that apply in relation to the capital that we are required to hold. We would make that judgment on that basis.

Q419 Dr Monaghan: With respect, a lot of the answers that you have given when it comes to the financial side of things have been quite ambiguous. When it comes to risk projection and weather maps and all the rest of it, you can be quite definitive. It does seem odd that you are definitive in one aspect of the business but quite ambiguous in another.

Brendan McCafferty: In relation to weather maps and modelling, we believe that we have done everything that can be done at this stage to understand the extent of the risk. We have allowed for the uncertainty, which is considerable in relation to mapping and forecasting. It is very considerable indeed. That is why, for example, we have a £2.1 billion reinsurance limit. That goes way beyond the easy assessment of known risk and allows for the uncertainty. Uncertainty is built into our understanding of the risk as well.

Mark Hoban: We talked earlier about the context of the £2.1 billion. In the 2007 storms there were costs for household losses of £973 million; for 2015-16, the cost was £459 million. We may be giving very precise answers but the scale of those losses demonstrates the magnitude of the uncertainty. Whether it is finances or risk projections, there is a huge amount of uncertainty built into that that we need to be resilient to.

Q420 Dr Monaghan: I just find it odd that, as insurers, who are normally pretty good at identifying risk and identifying levels of uncertainty, you do not seem to have very convincing arguments about what that uncertainty is and how it applies to the overall scope of Flood Re, the number of properties that may be involved or may not be involved.

Brendan McCafferty: Let me, again, take you back to the two weather events we have spoken about. If you looked at the 2015-16 storms, our view is that, if you took Storm Desmond, we might have seen maybe 40% of the risks that were inundated with water belonging to Flood Re.

Q421 Dr Monaghan: You are using the word “might” again.

Brendan McCafferty: Yes, because we have to assume, by working out what criteria we think insurers are using, what policies they would have sent to us. We cannot ask them definitively; that information is not available. We have to approximate, guess at and estimate professionally what risks we think they will send to us. If you compared that to Storm Frank, on the other side of the Pennines, the percentage was more like 25%. You can see, from just those two storms, that there is a very wide variation in all of the moving parts that allow an insurer, and therefore us, to know what share of the risk we would have borne in a particular event.

Q422 Dr Monaghan: I fully accept that there are parameters to the risk, but you have been asked a number of questions today where, quite frankly, I do not think you were able to identify the parameters. That is the concern I have.

Mark Hoban: Dr Monaghan, we launched on 4 April. We are two or three months into this. After a couple of years we will be able to give much more certain answers. Where we have risk on our book, we have seen the normal run of weather events and we have seen big storms, so we will be able to give a much clearer picture, as the business matures and develops. We are operating in quite a high degree of uncertainty here. I am pleased it comes across to you, because it certainly comes across to myself and the Board when we

think about the challenges we face. That is why levy 2 is in place. There is uncertainty about our ability in the early years to meet the cost of claims ourselves. Levy 2 is necessary. There is a lot of uncertainty. If you talk to any insurer, they deal with uncertainty. We have been through a regulatory process with the PRA and the FCA. They have to be comfortable that our model is resilient to cope with a wide range of weather events. It is the nature of the risk that we are trying to reinsure that creates that uncertainty. It would make my life a lot easier if we were a lot more certain than we are but we are not. We have to come to terms with that.

Q423 Dr Monaghan: In a couple of years' time, if Mr Parish invites you back, we can expect you to be a little bit more certain.

Mark Hoban: Absolutely. I am sure Mr Parish will invite us back and we would be delighted to do so.

Chair: Hopefully, if it is going well, we will not have to see you so soon.

Mark Hoban: Indeed.

Chair: If it is not, I suspect you will be back soon.

Mark Hoban: That is what we guessed, as well.

Q424 Chair: You talked about your launch on 4 April. I accept that it is not long but, anecdotally, when we were in Somerset on 12 May, there were people who said they were having difficulty getting insurance. Certainly, there have been articles in some of the major papers. Are you monitoring this all the time, because it is very necessary for you to be very proactive, especially through your early stages of birth and adolescence?

Brendan McCafferty: We are indeed looking at those experience every day. We can see in those areas, for example cases in Taunton, where there are 40% to 50% reductions in premium. We are looking at that systemically in the way that we run our business. We will be reporting on it externally at some point in the future.

Chair: Gentlemen, thank you very much. We are going to have the insurers in now so we will be able to check some of your detailed evidence. Thank you very much. It is nothing personal, but we are not looking forward to seeing you too soon because I am sure it will work. If it does not, I can assure you that we will be inviting you back very quickly. Thank you very much.

Examination of Witnesses

Witnesses: **Huw Evans**, Director General, Association of British Insurers (ABI), and **Iain Hamilton**, Head of Pricing and Underwriting, UK General Insurance for Personal Lines, Aviva, gave evidence.

Q425 Chair: Thank you very much, gentlemen, for coming along to our inquiry on flood resilience and particularly looking at insurance and reinsurance today. Could you introduce yourselves, please?

Huw Evans: My name is Huw Evans. I am the Director General of the ABI, where I have been a director for the last seven and half years. I helped negotiate the MOU that led to the establishment of Flood Re. I am also an unpaid director of Floods Re.

Iain Hamilton: Good afternoon. My name is Iain Hamilton. I am Head of Pricing and Underwriting at Aviva.

Q426 Chair: I have a fairly straightforward question to start with. How well did insurance companies perform over last winter's floods? I do not know who wants to start.

Huw Evans: I will lead on that, Mr Parish. I think the insurers overall performed very well. Our latest data that we have compiled, ready for release today, show that 90% of insurance claims have either been fully or partially settled over that period. We expected to pay out £1.3 billion in insurance claims, which will be the second highest in recent years, only after 2007. We know that we have also paid out £27 million in emergency accommodation and emergency costs. It is a very significant event. Insurers worked throughout the Christmas period around the clock, with their supplied partners, to help people both get into alternative accommodation and help businesses and homes cope with the immediate shock, and the rebuild process, which is always a lengthy one for such a severe flood, is now significantly underway. It will be a long haul to meet the full rebuild process for all those businesses and homes that were affected.

Iain Hamilton: From an insurance perspective, responding to those floods starts before the flooding happens. We have a major incident response team that is in place. We have a tried and trusted framework so that we are ready to respond to our customers before the events happen. In December, we had over 12,000 claims from our customers that we needed to go out and help. On the morning of the floods, we had people on the ground in the affected areas with command centres set up, so that we were able to talk to our customers face-to-face. For the first time, we used drone technology to survey the area of the damage.

Q427 Chair: Did you do that straightaway?

Iain Hamilton: Yes, on the morning of the event, for us to understand which properties were affected. That enabled us to contact some of our customers before they contacted us. Taking that proactive approach was key. In terms of dealing with the flood claims, no one flood claim is the same as another. We take an individual approach to repairing those flood claims. As a matter of course, we will always look to effect cost-neutral resilient repairs. The uptake of that is limited and there is some resistance from customers, but we have been doing that as a matter of course.

The other key aspect, in terms of what we have been doing in terms of the flooding, is also assisting our customers in gaining access to the grants. We recognise that process may not be simple and straightforward. For example, we currently have 48 applications that we are assisting our customers with.

Q428 Chair: Flood Re has stated that there is a changing attitude toward betterment. Does this mean we can expect to see reinstatement of flood resilient standards?

Iain Hamilton: In terms of our repairs, we will do cost-neutral resilient repairs as a matter of course. We have been doing that for a while. Where there is betterment, we will discuss with the policyholder or our customers how they can then gain access to those grants that are made available. We will help them with that process. One of the areas we would like to consider is how those grants could be made available to customers before the flooding has happened.

Q429 Chair: As far as the individual companies—perhaps this is where the ABI is concerned—have there been any companies that have struggled to find the necessary money to meet claims?

Huw Evans: No. The UK, as you would expect given it is the leading insurance market in Europe and the third largest in the world, also has some of the tightest prudential regulation in the world. This was not an event that affected any insurer in terms of its overall solvency; it was within the boundaries of what insurers would expect to pay, albeit it was a very significant event for the reasons I outlined. This is ultimately what insurance companies are for. This is why their businesses are run; this is why they are very heavily reserved and why they make extensive use of our world-leading reinsurance market—to enable them to cope with the shocks and the stresses, even when, as in this case, it happens within the last three weeks of the year. The impact, financially, is one that had not necessarily been anticipated for the rest of the year. Our insurance industry is extremely robust, very strongly regulated and has not suffered any prudential regulatory consequences as a result of these events.

Q430 Chair: You are an unpaid member of Flood Re, so perhaps you should declare an interest.

Huw Evans: I thought I did.

Q431 Chair: How do you see it working so far?

Huw Evans: I am an unpaid member of the Flood Re Board and my colleagues deal directly with Flood Re in terms of the operational relationship with the ABI, so there is a bit of a Chinese wall within the ABI, as you would expect. I have nothing but admiration for the team at Flood Re for the immense work they have put in over the last three years to build a world-first project. There is nothing simple or straightforward about doing something for the first time of this nature. Public-private partnerships, as you will understand, are complicated and challenging. Government often finds it difficult to relinquish a degree of control to an external body, even a not-for-profit one that is trying to do something new and different.

The regulatory submission alone, to be approved, was 62 huge documents that involved 18 months' worth of dedicated work. It is easy to underestimate just how much work had to go into getting Flood Re up and running. The fact that it succeeded, was ready and worked on day one is a very significant credit to the Flood Re team and the insurers who worked with it to have it ready. As Mark Hoban and Brendan McCafferty said, that is just the beginning. The test for Flood Re in the medium to longer term is to meet its statutory

objectives, but they did extremely well to meet the challenge that was laid before them and to build something that had never been done before from scratch that worked on day one. I am sure there are many Government project managers who would like a bit of advice on how that could be done.

Q432 Chair: And as far as Aviva is concerned.

Iain Hamilton: In terms of how Flood Re is impacting our customers, it is early days. We are seeing very positive customer messages coming through. We are getting customers who are now able to purchase a premium online directly with us. Beforehand, we may have asked that customer to come and talk to us around what measures may then make that risk acceptable. In terms of premiums, we are seeing customer premiums in high-risk flood areas for new customers reducing by circa £500, which, again backs up the affordability part. We have seen an individual customer save well over £1,000. We have had a good story from another customer who was not previously able to access flood insurance; they have been able to purchase it for the first time.

Chair: I will stop you there, because we are leading into Margaret's question.

Q433 Ms Ritchie: Gentlemen, Flood Re only came into operation, as we know, on 4 April. There has yet been little data on the impact on the availability of affordable policies. Press reports have cited significant quota reductions for some, although anecdotally problems remain. In that respect, how are insurance companies applying Flood Re to insurance policies for people in flood risk areas?

Huw Evans: Perhaps if I answer for the industry as a whole and let Iain cover Aviva specifically, as one of the leading players in the market. As Brendan noted, and he was right to do so, this will take time for Flood Re to build up to its full capacity. It will take time for the market to adjust to be able to take full advantage of it. It will take time for customers to build understanding and awareness that Flood Re exists and to be able to know how to access it. Perhaps that references some of the individual studies you came across in Somerset. It is taking time for some of the comparator websites through which many people buy their insurance to fully integrate with Flood Re and be able to offer the full range of insurance policies.

To a certain extent, those are some of the trade-offs that had to be made for it to be ready on day one and working. You accept a phased build up, rather than a big-bang approach where you wait until every single insurer is ready, every single comparison website is ready and then you flick the switch. The decision was taken instead, quite rightly, to get on with that and start with those who are willing to offer services to customers from day one and build up capacity over time. It has had a good start. Where there are individual cases of either customers not having access to it or insurers still building their systems to take full advantage of it, that is definitely within the boundaries of what we would have expected for the first few months.

Q434 Ms Ritchie: How much data are being released on how Flood Re is being applied to customer's policies?

Huw Evans: That is clearly something that Flood Re is collecting at the moment. You had a firm assurance, which the industry would support, from the Chairman and Chief

Executive of Flood Re, that the data it collects will be publicly available, as you would expect for a body that—

Q435 Ms Ritchie: What is your assessment of the situation because you are answering it as if you were a representative—if I may say so, with a level of temerity—of Flood Re. What is your assessment, as the Association of British Insurers?

Huw Evans: We will largely rely on Flood Re for the data because they are best placed to provide it. Certainly, anecdotally, our sense, if we go on the postbag alone, from MPs, which is a fairly reliable barometer of the extent to which there is a problem, that postbag has dropped to virtually nothing in terms of MPs complaining that they have individual homeowners who cannot get access.

Q436 Ms Ritchie: It is very early days.

Huw Evans: It is very early days yet, so that caveat would apply.

Q437 Ms Ritchie: May I ask Aviva how companies, Aviva being one of them, are assessing whether households are in high-risk areas and what supplementary assessments have you done? What discussions have you had with the Met Office, the Environment Agency and other likeminded bodies about potential for the future in terms of floods?

Iain Hamilton: I can only talk on behalf of Aviva. We have a tried and trusted understanding of flood risk that we have been developing for a number of years. Back to one of the earlier points, we assess flood risk at an individual property level and we are not at the level of detail where we can understand if that entire property or parts of the property will flood. In terms of our understanding flood risk, we continue to use external data sets that are available through organisations such as JBA. We are using that data and continue to use that data to understand flood risk. We will use that in our assessment of understanding whether it would be beneficial for us to cede that customer to Flood Re so that we can offer them a cheaper premium.

Q438 Ms Ritchie: Do you intend, as a company, to make data on their application of Flood Re to customer policies available? It is a question around the issue of transparency: do you intend to make that information available on how you apply Flood Re to customer's policies?

Iain Hamilton: Being transparent is one of the key areas we focus on to our customers. In terms of when a policy is ceded to Flood Re, the customer relationship is still with us as an insurer. They see no change in the way their policy operates and, indeed, how any claim operates. There is no differentiation in terms of that service. On their policy documents, it will be clear that we have ceded that policy to Flood Re and they will be signposted to our website where we give them more information around what Flood Re is and what that means.

Huw Evans: From an industry perspective, it is an interesting point: the balance between transparency on the one hand and the market sensitivity of data on the other. With your permission, it is worth drawing out a little bit. We would expect, over time, Flood Re to say how many policies had been ceded into it and for that data to be publicly available. However, which companies have ceded how many policies is market-sensitive, because it is a market decision for each company how much they choose to use Flood Re and the extent to which they use the reinsurance that Flood Re offers and the extent to which they

use their own reinsurance. I do not think we would expect to see Flood Re publishing, for example, a breakdown of every single firm and how many policies it had issued or, indeed, for those firms themselves to put that data in the public domain. That is part of a commercial decision-making process, which would potentially influence the behaviour of its competitors.

Certainly, the Flood Re Board—wearing my other hat—is very conscious of the market-sensitive data of some of the information it has ceded, even in projected terms only, about how much each firm may use Flood Re. That is where there is a boundary between the fact that, on the one hand, this is designed to be a public good and is publicly funded so requires a degree of transparency and accountability for that, but on the other, it is also a market mechanism designed to help a commercial market function more effectively for customers with the sensitivities that come with that, in terms of competitive dynamics and so on.

Q439 Chair: Perhaps to Aviva this is a market-sensitive question, but to what extent do you target insuring properties that could be potentially prone to flooding? Do you have a percentage of that because you have to run your company with a share of risk? Do you make a conscious decision on whether you actively go out into the market seeking those areas or not? Do you price your policies in a certain way and then you do not know how many of those properties you may or may not have that are potentially prone to flooding?

Iain Hamilton: Before the invention of Flood Re, your marketing decisions are not based on whether you are in a high risk flood area or not; it around whether you get economies and efficiencies of scale in terms of marketing spend. Now that Flood Re has been introduced and, in the event we were able to offer a competitive premium that is affordable, I would see those customers not being excluded from marketing communications. We would not definitively go out and target those areas per se.

Huw Evans: It is a really important area to probe because the point of Flood Re is to help the market work better than it worked under the statement of principles. What the statement of principles did was freeze in time insurance companies' flood risk as of 2000, when the statement of principles was agreed with the then Government. The big companies' flood risk was dictated by who they had on their books at that point. You had an unevenness in the market. Newer players would come into the market they were refusing to offer cover to any flood risk customers; why would they? The older players had this large block of customers who were then being charged increasing levels of cost for what they had. It was a very, very unsatisfactory market. It was not working well for customers at all. That was why the first Government, after many years of arguing, and then Parliament was convinced of the rationale for Flood Re. It enables the market to operate much more freely. Any firm can target any customer knowing that if they have a high flood risk, they can send that element of the risk over to Flood Re. It helps the market work in a much more fluid and free way. I would be very surprised if, as a result, firms that previously tried to avoid customers with high flood risk therefore did not participate fully in the market.

Q440 Chair: So you think this should encourage them to enter the market. If it does, it will create greater competition and hopefully lower premiums.

Huw Evans: I am very confident that will happen, if it is not happening already.

Q441 David Simpson: There are two points to the question I want to ask you. You will have heard some of the points that I made to Flood Re in relation to the transition period and the smooth transition. With yourself being an unpaid director of the Board, what is your view of that? You have two pictures, from one side and the other, of the whole transition. What is your view on that?

Huw Evans: I remember very clearly the negotiations that led to the setting up of Flood Re. It was always a desire for Ministers—and I think this came through quite well in the parliamentary debates that then followed with the Water Act and the secondary legislation—that parliamentarians, and indeed Ministers, were keen that Flood Re did not just provide a 25-year sticking plaster and that nothing changed during that period. Insurers were keen for that, too. Insurers did not want to spend £20 million and thousands of people hours setting this thing up for it to work for 25 years and then return everyone back to the same position at the end of it. The transition piece is significant, important and has a couple of components. There is definitely a piece around building consumer understanding in education, so that consumers who are flooded take the options for resilient repair that companies like Aviva offer them and become more aware of flood risk, preferably when they are buying their properties. There is also a piece that allows time for our planning and investment approaches to water management in this country to change quite fundamentally. It is very, very difficult to do that on a three-year or five-year cycle. A 25-year cycle allows time for Government, local authorities, the Environment Agency and others to create a better system of water management, of planning and of customer awareness than we have at the moment. The transition plan that Flood Re produced is a starter for 10, if you like, as they would describe it, in terms of beginning that process.

It is why the work that Oliver Letwin is doing and you are doing in having inquiry is so important, because we have to seize this opportunity to have a better system. We may not want to go the whole way of the Netherlands, in terms of having a whole system that is designed around water management but, boy, if we could go a long way, from where we are now to even halfway towards that, that would result in a much better, more holistic effective system for the way in which we manage land, manage our water and the way we take planning decisions. That is the opportunity that we have.

Q442 David Simpson: It is a work in progress.

Huw Evans: Inevitably. I very much hope it is work that gets done because it would be criminal to miss the opportunity that Flood Re offers.

Q443 David Simpson: It certainly would. The other point that I raised, and Margaret touched on it in her question earlier, is in relation to the whole issue around transparency, and you will have heard what I asked Flood Re in relation to individual policies with the general public. From your own point of view, Iain, maybe you could answer this: in relation to the policy and how transparent it is, the small print and all of that, it is worrying, to a certain degree, that Flood Re had said that they had no remit when it came to the policy itself. In dealing with the public, there was no hotline to them. It was between the public and yourself. How can we be assured that we are not going to go back to the same old same old again, of, “Sorry, you have applied for a policy. You are not going to get it.” The whole idea and objective is to try to help the people get a policy and have that assurance. Nobody wants to be flooded but if they are living in that area it is going to happen. It is about that assurance

that they are not going to be pulling their hair out. How are they going to resolve this? How open and transparent is all of it, including the small print?

Iain Hamilton: From an Aviva perspective, in terms of transparency we have taken a proactive approach with our customers and contacted customers in high-risk properties to make them aware of Flood Re. For existing customers, if they have contacted us to see whether they could cancel and benefit from Flood Re, we will do that and we will not charge them a cancellation fee for that. In terms of transparency of policy wordings, that is one of the core things we look at and measure on a regular basis in terms of customer dissatisfaction. We regularly look at areas where customers are making claims or submitting claims that may not be covered under the policy. That is one of our key objectives: to make sure customers understand what they are buying. The final stage of that process is we do not take turning a claim down lightly. We go through a rigorous process. If a claim has gone to the Financial Ombudsman, we will work with them to understand the best solution.

Q444 David Simpson: In assessing the policy with an individual customer, do you take into consideration how objective they have been in trying to protect their homes, or is it just based on A, B and C? Is it a historical thing? How do you do that?

Iain Hamilton: One of the key areas is understanding what information is available from the customer. In a typical online journey, there are only so many questions you can ask. At the moment, we are reliant on the customer providing us with additional information, so where additional measures may be in place, it is for the customer to talk to us and tell us about those measures. If I talk about businesses, particularly large businesses, what we would tend to have is our own risk surveyors go out to those properties and, first, assess the risk measures they have in place, and, secondly, we will discuss with them what measures would make a tangible difference to their risk and also insurance premiums and excesses.

Huw Evans: From the wider insurance perspective, I agree that, from an ABI perspective with Flood Re, the primary relationship has to be between the insurance company and the customer. That is where the contract exists. They are the people who have the primary ability. As the ABI, we have a representative role; we have more of a role than Flood Re, actually, to help inform customers and try to shape the weather—if you pardon the pun—so that customers have a better understanding of what is included and what is not. Transparency is an important part of that. For the first time, this year we have published industry data showing how many claims get paid. That showed that while nearly 99% of motor claims were paid and over 90% of travel claims were paid, that figure was 80%—eight out of 10—for most homeowner policies.

There are two main reasons why claims do not get paid: first, things do not get covered, most typically when storm damage takes a roof of a shed or something and the customer has bought quite a cheap policy that does not cover their outbuildings. That is a very, very common reason for a claim to be declined. The other is that they have not maintained their property. Nobody has been up on their roof for 25 years and then it starts blowing off. At that point, the insurer will potentially decline the claim. We know, on the whole, why claims get declined. There is not a vast array of reasons. They tend to be around those two areas. That is why we are trying to do something about it.

The ABI published yesterday a new homeowner's guide to try to help homeowners understand—in very, very simple terms—what it is that they need to do and how they need to approach their insurance policy. Yes, there is more to do about helping people understand the small print, both with regulators to allow insurers to make things simpler, because that is not always straightforward, but also to explain it in language that people understand. That is our responsibility as an industry. It is also one shared with customers as well. They do not buy their insurance in five minutes on a comparison website while watching the telly; they pay attention to what they are buying and make sure it meets their needs. That is absolutely critical.

Q445 Chair: It is early days and you are three months in, but Flood Re has 23 years to run. The positive part of it is at the moment it seems to be working pretty well. Is there going to be a little bit of complacency, now it is all working well, in how we move out of Flood Re back into the market. How are we going to deal with that?

Huw Evans: When we struck the agreement around Flood Re, that was one of the thoughts we had about the importance of the five-year statutory review that takes place. That is to ensure that it does not drift into, as you say, a period of complacency over the middle years, because every five years there is a fixed point where you as parliamentarians, the Government, the Treasury, and the Board of Flood Re have a statutory responsibility to take stock of how it is going, not just on the financials, which we discussed just now, but in terms of how the scheme is working, how effective it is and, critically, back to the point around transition, how well the time is being used to effect change in the way in which we manage water and flood development.

Q446 Chair: Do we need to make sure that we properly monitor it every five years, rather than let it drift?

Huw Evans: It is a critical part of the design to ensure that it does not drift. Of course, it is not the only thing. Speaking as a director of Flood Re, we take our responsibility as directors very seriously; this is a very important undertaking, not just because of the amount of public money involved but because of the need to ensure that every year of this 25-year period—in fact every month of that period—is used wisely and effectively.

Q447 Angela Smith: You mentioned the Netherlands and we were there last week. We saw for ourselves some of the measures taken by properties in unprotected areas to help defend themselves against potential flooding. This is a key factor in the Flood Re scheme: flood resilience on the part of individual properties. How are insurers promoting home resilience measures? Are you reducing premiums and excesses for those who do go to the trouble of installing such measures in their properties?

Iain Hamilton: In terms of flood resilience measures, I mentioned earlier the procedure as a matter of course as part of our repair process. We will look to effect cost-neutral flood resilient repairs wherever that is acceptable to the customer. We also, as part of that repair process, where the grants are available, are assisting customers in trying to apply for grants to put in place additional resilient measures. Two or three areas of the resilience measures are that the grants are only available to customers once they have been flooded—we would welcome those grants being made more widely available before that event happens—and, secondly, there is not a common standard in terms of those resilient

repairs. In terms of assessing the risk benefit of that, it makes it more difficult for us. Where there is a risk benefit, we will pass that through in terms of customer premiums.

The third point is that with the resilient measures, the key benefit to the customers is getting them back into their properties quickly. We have certainly seen that in some of the recent floods, particularly in December. We had a family: two elderly parents and two grown-up sons living with them who were disabled. They were a close-knit family. One of the key concerns with them is that they needed to stay as a family unit. We worked hard with them to try to find a suitable accommodation that could meet their needs and facilitate them. One of the key concerns was how quickly they could get back into their property. Whilst we use the latest drying techniques, we found that there were some resilient measures in place in that property. That meant that, from having the claim in early December, they were back into their property early February. That is the key benefit to customers: the trauma of being out of their homes and not necessarily the premium benefit.

Q448 Angela Smith: You mentioned standards. We need a standard here in order to help the insurance industry and make accurate assessments of risk and so on. Whose responsibility is it to develop that standard?

Huw Evans: It is something that we would like to see the Government taking on, because we think that, with the whole resilience piece, the Government have been right to make money available. We have always welcomed it and the industry has worked hard to try to spread the word, albeit it has been quite difficult. There are some flaws in the way in which it is currently done: there are no fixed standards, and it is something that could be done. There is no fixed piece of advice that the Government get their weight behind to help customers understand the benefits; it is something that is done on quite an ad-hoc basis. Of course, it is not a centrally driven scheme. A pot of money comes from central Government but it is then delivered locally with a series of local objectives and a local implementation framework. Our view is it would be much, much more efficient if it were a centrally co-ordinated framework, with a central criteria and a central set of standards for qualification advice, delivered through local authorities who are best placed to do it, rather than being in the position we have been in now with the last floods, where each local authority is doing it in a slightly different way and working out how to meet its statutory value-for-money criteria in the administration of the grants. We think that is something that should be done by central Government, with the responsibility of the local authorities purely being to get the money out to the affected areas, rather than the onus of proof being on them to make sure that the money is being spent wisely.

Q449 Angela Smith: The standard relates to the grants but what we are trying to get at with this question—and I take that point entirely; it is a valid point—is whether or not the insurance industry can help incentivise the installation of flood resilience measures by offering lower premiums and by, potentially, as you heard in the earlier evidence, not insisting on like-for-like replacement when people are flooded.

Huw Evans: It is easier for the industry to reward people than to incentivise them. Why? Because three quarters of people shop around for their home insurance every year. You could very easily be in a position where insurer A has put money up front to help homeowner A make their property resilient. Homeowner A then goes to insurer B the following year and insurer A gets no benefit whatsoever from having helped that

customer. Insurer B, who did not pay for it, gets the benefit. In a market like ours, where people shop around for their home insurance all the time, it is quite difficult to do incentivisation but it is more straightforward to do reward. As Iain said, insurers will look favourably—why would they not?—on somebody who has put resilience measures into either their home or their business because it means a quicker drying-out process and probably a cheaper repair.

Angela Smith: That is what I meant by incentivisation.

Huw Evans: It works much better as a reward. Any standardisation in this arena, whether it is in terms of the quality of building work that is done or the process that is done to allocate the money, would be welcome as we go forward. Regarding the resilience grants that the Prime Minister announced back in 2014, at the time when it first ever happened, nobody was sure if it was a one-off, but with the winter floods that then followed last year, the Treasury made very clear it would put that money up again through Defra. We are now in a position where we can be comfortable that the Government are going to feel they have to put that money forward each and every time. Therefore, we should move to a greater standardisation approach.

Q450 Angela Smith: I take the point entirely about grants but I am not quite sure I like the continual falling back on the grants system. Surely the insurance market itself ought to be able to provide the rewards-based approach that you have talked about, whether we call it rewards or incentives. In the end, if the market works properly it ought to be able to price products according to how much effort people have made to protect themselves.

Huw Evans: I absolutely agree we have a role. I am not trying to walk away from that for a moment. I am just reflecting the reality, which is that the thing that has had most cut-through with customers so far is the offer of a grant from the Government. Insurers have spent many years trying to engage customers in resilient repairs. The thing that has had most cut-through to those customers has been when the Government have started to offer a financial contribution towards it.

Q451 Angela Smith: Leaving the grants to one side—and I take the point again—how much more do you think you can do by way of advertising your products to customers to make them aware that, for a small investment, they can perhaps get lower premiums? Do you think you are doing enough?

Huw Evans: There is always more you can do. We have just published a new guide on homeownership. We, the ABI, have taken a much more proactive role in the last few years, including the Flood Free Homes campaign, which many of you supported, to try to drive different ways to get through to customers to help them understand flood risk and what they might need to do towards combating it. I would accept there is an ongoing challenge there to the industry to do as much as it can. That is something that the industry accepts collectively, but also the individual firms will seek to do using their own marketing budgets that are obviously much more significant than those that the trade body has.

Q452 Angela Smith: Do you think like-for-like ought to change? Is it a barrier? Perhaps insisting on like-for-like is not helpful.

Huw Evans: My sense across the industry—Iain can speak for Aviva specifically—is that like-for-like is less of an issue than it used to be. Insurers are much more flexible now in terms of working with customers about what they want in terms of the restoration of their property and the re-creation of your property, rather than a very rigid tick-box formula that says they can only have what they had before. It is quite common. You may have seen this on some of your visits. It is quite common, when people have been flooded, that they say, “You know what? I do not want my old kitchen back; it was on its last legs anyway. If I make a contribution towards it, can I have what I would have had for the old kitchen and then I will put some money in and I will get a new kitchen while we are doing all the work.” That is a very, very common approach these days, and much more common than a tick box like-for-like approach.

Iain Hamilton: From our perspective, it is a customer-led claims process. To talk about flood claims, what we do is we will work with the customer and we will understand what they want. Absolutely, if that is like-for-like then we will give them like-for-like. Where we can effect cost-neutral resilient repairs, if that is something they are open to we will do that. However, if they want to upgrade or even change things—perhaps they want a different kitchen—we will work with them and pay our contribution towards that and allow them to upgrade should they wish to do that.

Q453 Angela Smith: That is really helpful. Finally, should we change the building regulations so we can make sure that all properties are flood resilient in future?

Huw Evans: I would certainly support anything in the building regulations that encouraged greater resilience and greater sustainability of new-build developments. It is something the insurance industry have been calling for for a long time. It is a point of frustration we have with the current planning process that there is a bit of an information void about developments that go ahead against Environment Agency advice. It is very difficult to know how many of those there are and there is no central database, because it is not mandatory for local authorities to report those decisions back to the EA. There is no central database where those decisions are taken.

Q454 Chair: That is an interesting point you make, and we might record it in our report.

Huw Evans: A very big hole in the data that policy-makers have, as well as insurers, is how big a problem we have here. It does not provide any disincentive, as you would hope, for developers who are tempted to do development on the cheap with cheap sustainability. Even if they persuaded the local authorities to go ahead, if they think the knowledge that that was built against EA advice is going to disappear into the ether, then they are going to be encouraged to work it that way.

Iain Hamilton: I would, potentially, go one step further there, in terms of being able to pass that information back to insurers when we are making our decisions. If a property has been built after 2009 but has resilient measures in place, currently we are reliant on the customer to offer that up for us. In a car quote, you would just put in your registration number and we would know, automatically, that it has all of the various safety features. Could there be a database that insurance could link into so we are not reliant on the customer giving us the information to take that into our view of risk?

Huw Evans: At the moment, insurers cannot get that information out of the Environment Agency because the local authority is not mandated to provide it to the Environment Agency.

Q455 Chair: I have just one final point. You talked a lot about “cost-neutral”. If you had a flood, it seems to be a logical improvement that, the next time you make repairs, you put the sockets up above a potential flood area. How do you go about encouraging people to do something basic like that if it is going to actually cost more? I accept that they can go to another insurer afterwards but not going down that route would be a missed opportunity. What do you do as an insurance company? I ask that to Aviva particularly.

Iain Hamilton: It depends on the claim, etc, but we would look at things like waterproofing, damp-coursing, waterproof plaster and those types of things, depending on the cost of the claim. You can look at things like stainless steel kitchen units. It is all very much driven, though, by the customer and what they are open to. We can tell them what sorts of things we can provide to them on a cost-neutral basis and what sorts of additional measures they could put in place and at what cost.

Q456 Chair: Just to pick you up on waterproof plaster, we used to render most of our walls, did we not? Now we actually put plasterboard there and just cover it. Of course, there is nothing worse than plasterboard; as soon as you get an ounce of water on it, it disappears. Are you actively doing something about that as well?

Iain Hamilton: We encourage having waterproof membranes and things like waterproof plaster.

Q457 Chair: Even if it is going to cost more? You said everything had to be cost-neutral. That is the bit I am really drilling down on.

Iain Hamilton: Yes. We will work through what measures we can put in place from a cost-neutral perspective and then we will discuss with the customer the other measures that may be available to them and what the costs would be.

Q458 Chair: Would you share some of those costs in order to give them an incentive to go down that route? I do not know whether you can within the market rules, but could you say, for instance, “We will share the cost of this and we will give you a discount over a period of years”? Can you do that, tying them in to you as an insurance company?

Iain Hamilton: At the moment, we do not do anything in terms of betterment in terms of the claim settlement. Where we are able to give them the benefits of our scale and our purchasing power, such as discounted kitchen units, for argument’s sake, we will pass on those benefits of our scale to the customer so that they can purchase those things at a reduced rate. It is an interesting point that you make there around whether there is a longer-term opportunity in terms of upgrade.

Q459 Chair: It seems like a missed opportunity if we do not go for it.

Huw Evans: The nature of household insurance, and indeed business insurance, is that it is an annual contract, so it is very difficult to do that spread over five years in the way that you might with a different type of legal contract. Certainly our experience—and I saw this for myself in Carlisle before Christmas—is that there are very active, engaged

conversations taking place between customers and insurers about the trade-offs and the choices that are available in terms of what they can get for their money and what resilient repairs they might want to do. Certainly, in those areas that have been flooded more than once, there is quite a high degree of appetite from customers for the construction to take place in a way that can minimise how long it takes them to get back because they have been through it once before.

There is also a slight difference between business premises and homeowners that is worth drawing out. Business owners are often a bit more willing to take steps along these lines because it is a business premises rather than a home. In York, for example, many of those businesses that are near the river have been flooded many times, and those business owners have a very sophisticated understanding of resilience measures and have very engaged conversations with their insurers, whereas a homeowner, who may have only ever been flooded once in an area that has no history of flooding, will often be quite resistant to having sockets halfway up the wall because they say, “It tells people that my house is a flood risk and no-one will ever buy it”. There are some concerns there that you have to try to overcome; sometimes you can and sometimes you cannot.

Q460 Dr Monaghan: Outside of Flood Re, what can we do to make affordable insurance available for all businesses?

Huw Evans: There are several things that could be done that do not involve trying to dismantle and rebuild Flood Re. The first thing is to develop a greater market for SMEs that have a problem. Flood Re referred to a scheme that is being developed at the moment, which is a market-based solution with the London market fronted by the British Insurance Brokers’ Association, which they hope will go live in October. That scheme would offer availability but it would not touch affordability. None the less, there is room for a greater specialist market to develop.

There are some preventive issues that could be tackled which would reduce the number of SMEs that have a problem getting cover. For example, the current formula that is used to justify flood defence spending, as you are no doubt aware, actually favours protecting homes slightly above protecting businesses. That does not necessarily help in terms of reducing the number of SMEs that might find themselves in that position.

If all of that still does not tackle what is still quite a small problem—but obviously a very big problem for the businesses affected—I would like to see Government-backed approaches. There are two things that the Government could do which they currently do not. The first is to offer a type of pay-out scheme, as it does with export finance insurance, where it recognises that the insurance industry cannot provide any cover to people engaged in quite high risk export business, and so it offers a form of insurance that offers a fixed pay-out if there is a claim. That is better for Government to manage rather than an insurance company because it can manage its costs better. It is also worth noting that, in education, the Government has actually set up its own insurance scheme for academies, despite the fact that there was a fully functioning market that was working perfectly well in providing academy insurance. The Government actually decided to set up their own scheme, backed by the Department for Education, to provide cheaper cover than was available in the market for academies.

There are things that the Government can do, which they already do in terms of providing insurance cover, if they want to. Finally, if they wanted to, they could offer very selected targeted grants for small businesses that were suffering with high insurance costs. Those are all areas that have not yet been fully explored but which would provide a potential answer to the relatively small number of SMEs who are finding that their insurance costs are unaffordable.

Iain Hamilton: From an insurance perspective, we are proactively involved in those discussions at an industry and Government level on any wider solutions, and we are proactively participating in the Defra and BERG forums that are taking place on this particular subject. In the meantime, we are continuing to renew customers in high-risk flood areas. We are committed to not applying excessive increases to those small businesses. We are not applying large increases to excess at the first renewal to those people impacted by floods. In particular, for large businesses, we are continuing our current approach, which is that our risk assessors will go out to those businesses and work with them to understand what measures they could put in place to help make a tangible difference to their flood risk.

Q461 Dr Monaghan: Do they get a rebate or a reduction in their premium for that?

Iain Hamilton: We will talk through flood measures with them in terms of which things will make a tangible difference to them getting back into their properties as well as what that may do in terms of their premium and/or excesses.

Q462 Dr Monaghan: Iain, in the written evidence from Aviva that was given to the Committee previously, it was suggested that there should be an independent study into the affordability and accessibility of flood insurance for SMEs to measure the scale of the problem. How would you like to see that work and what format would it take?

Iain Hamilton: It needs to be a study that works for the industry. There is a point there around understanding whether there is a systemic issue within that segment and then using that information to inform the ongoing conversations that Huw mentioned.

Huw Evans: There was a Defra study last year that found no evidence of a systemic problem, and that is our assessment too. That is not to say, of course, that those individual SMEs that are having major problems are not in a significant bind. We try to deal with them and we work with them. We try to point them towards specialist brokers who know where to look in the insurance market to find them cover. We are not saying that there are not some businesses out there that are struggling to find cover but we are not in the same position as we were with the statement of principles, where you had hundreds of thousands of homeowners who would otherwise not be able to afford their insurance policy, which required first the statement of principles to be put in place and then Flood Re. The two are not comparable, and that is why, in our view, we are better off looking at slightly more targeted policy solutions to deal with SME provision.

Q463 Dr Monaghan: Would you both agree that there is an affordability issue for some businesses, and potentially for a significant number of them?

Huw Evans: We cannot get away from the consequences of 30 years of under-investment in flood defences in this country and a planning process that still does not protect

homeowners and businesses enough against poor development and insufficient flood protection. This has been a long-running sustained problem for this country that we are only beginning to wake up to in recent years. Frankly, it was only when the ABI, negotiating on behalf of the insurance industry, insisted that it would not sign the MOU for Flood Re that the Government agreed to re-instate the money taken in cuts to flood defence spending that had taken place in 2010. It is not the case that we are living through a golden period of investment. We very much welcome the investment that has been put back in place, and that is a good place to go from, but there is a huge amount still to do in this country in order to have an optimal system of water management planning and flood defence investment that will genuinely offer the best possible protection to businesses and homeowners. Until we are in that position, there will always be a small number of businesses that are adversely affected by the consequences of not having had that long-term investment.

Q464 Chair: I accept that the Government does need to take its share of responsibility but surely you also have to take a certain amount of responsibility because you are insurance companies and you should be insuring risk. There is an argument that all you want to do is shift the risk on to the Government and take all those areas that have no risk.

Huw Evans: It is quite the opposite, actually. Clearly, the more customers the insurance industry has, the better. The insurance industry would like to be in a position to offer cover to everyone who wants it. Those are customers; no business wants to turn away potential customers. In fact, in the area that I mentioned where the Government did step in to provide insurance cover with regards to the academies, it was actually taking away what was a very healthy market where the insurance industry was doing its job in offering cover for academies up and down the land

Q465 Chair: I am conscious of the time so perhaps I could rephrase the question: could you also contribute as an insurance industry towards some of those schemes? If you are critical of what the Government are putting up, surely it is in your interest as well, is it not?

Huw Evans: We have, of course, invested over £20 million and thousands and thousands of hours of executive time in setting up Flood Re, so I think we have made a fairly significant contribution, quite rightly, to economic and civil society in terms of trying to provide solutions rather than just complaining about things. The primary responsibility for trying to tackle these specific issues has to come from Government but the insurance industry will continue to play an active part in this, and that is why we are here today. We welcomed this inquiry and submitted detailed evidence because we want to have a healthier, better framework in which these issues can be dealt with naturally by the market without any further need for intervention.

Q466 Chair: If you are a major company that has a lot of properties in a flood-prone area then surely, if you actually made some sort of contribution, it would help put the money together and then that would potentially save you money. Do you not want to go down that route?

Huw Evans: Nobody has a magical pot of money that nobody else has contributed to. If an insurance company makes a contribution, that is something that its other customers have to pay for. We had that debate very openly with regards to Flood Re and Parliament discussed it extensively and decided that it was comfortable with that degree of cost

subsidisation. In my view, there should be an open public debate about the extent to which that is allowed. I do not think that insurance companies putting £10 million here or £20 million there towards a pot of money, without the consent of their customers or a debate in Parliament, will make the problem go away. I do not think that is a terribly healthy way to operate and I suspect their shareholders will have something to say about it. It is far healthier to have these open debates about, if cross-subsidisation is required, to what extent it is justifiable, but also to say that the solution should be proportionate to the scale of the problem. We do not believe there is a wide-scale, systemic problem with SME access to insurance. We therefore believe that the best solutions are likely to be small-scale and targeted rather than of a big nature such as Flood Re, which was the appropriate solution for that.

Q467 Dr Monaghan: That was an interesting point that you made there. Iain, do you have anything to add to that argument?

Iain Hamilton: I would support what Huw has said. There is no evidence to suggest that there is a systemic issue at the moment. Would a cross-subsidy solve that argument or solve that problem in terms of the costs of actually putting flood defences in? I suspect it is quite small in terms of the actual cost of building those defences. However, we would proactively work with the ABI and Government in finding what a suitable solution might be.

Q468 Chair: Regarding the provision of affordable insurance for those properties built after 2009, do you have any idea how many properties fall under that category and whether most of them are insured, or whether they insure at all? Do you have any idea what the situation is?

Huw Evans: There is no reliable industry-wide data. It is obviously very difficult to gather data on something that is not insured. Certainly, when we were negotiating Flood Re and Parliament was discussing the exclusion, there was no reliable evidence put forward about the scale of the problem. In the absence of any hard data you often have to rely on MP postbags to get a feel of the issue, but we really only ever dealt with two or three MPs who had a problem in their constituency with a development that fell outside the exclusion. However, the exclusion was there for a very important reason, which was to stop a closing-down sale from the point at which the MOU had been agreed in 2013 over the three years that it was going to take to build Flood Re. The last thing we wanted to do was inadvertently incentivise developers to rush through developments in flood areas, the insurance bill for which they would then pass on to the rest of the taxpayers through the Flood Re levy. That is why the exclusion existed. Clearly, there is a five-year review period, as we have already discussed. That is the appropriate point to take stock of whether it is still needed or not.

Q469 Chair: On the question of how the industry would provide insurance, I take it that that would be done entirely on risk and could not be put into the Flood Re system. What you are saying to us is that you do not see it as a major problem. From Aviva's point of view, do you get many people asking you for insurance for properties that have been built after 2009?

Iain Hamilton: The market for those properties, from our perspective, will operate as the whole market had operated before Flood Re, so it will be a risk-based approach for those customers. For our existing customers, we will continue to renew them and, actually, we

have removed the excesses across all of our customers, regardless of whether we concede that business to Flood Re or not. Does it answer the question on affordability and accessibility? No, and that is why Flood Re was pulled together. The key point comes back to the planning process: how many properties are actually still being built in high-risk flood areas and what measures can be taken to ensure that that is resolved going forwards. Certainly from our perspective, we have just launched a home risk checker, which enables customers to go onto our website, put in their address and get our view of the flood risk for that property. It is only a small step we are taking, but clearly wider measures are needed.

Q470 Chair: That helps people who may or may not be buying a property, but it does not necessarily help anybody who is actually living in a property built after 2009.

Huw Evans: No. Going back to what you could do over the 25 years, one of the things you could do is to make it mandatory for estate agents to have a traffic light system that encourages people to understand the flood risk in the area in which they are buying so that, ahead of doing the searches after they have already agreed a sale, the consumer is better informed.

On the 2009 issue, my judgment is that the other reason why it may not have been a bigger problem is of course the economy was in a recessionary state during that period and house building was very suppressed. There was therefore less house-building going on during that period from 2009 to 2013 than you would have expected in a normal year and I suspect that that may have affected the supply. My judgment is that most of the relatively few homes built in that period were insured. Some of them would probably be a bit cheaper if they were inside Flood Re but there is not a widespread problem of access to insurance for those properties.

Q471 Ms Ritchie: Just for clarification, are insurers, or your broad membership, developing policies specifically aimed at houses built after 2009?

Huw Evans: Not specifically but they are covered by the market anyway because, of course, the exclusion only applied to Flood Re rather than the industry as a whole. There was no moratorium on the industry providing insurance for those homes; it just purely carved it out from Flood Re. The market at the time—I remember it well—was confident that it could absorb the relatively modest number of homes that may be affected and that, while they may not get the best possible deal because they are outside Flood Re, they would still get affordable insurance. There has been no evidence presented to me that has ever contradicted that that happened as a market dynamic. Iain's sense from one of the biggest firms was that those homes can get insurance.

Q472 Ms Ritchie: Are you aware of whether the decision to limit Flood Re to houses built before 2009 has had an impact on house-building in high-flood risk areas?

Huw Evans: It is difficult to know because of the point I raised earlier: we have this information void around development in high-flood risk areas. If there is anything that comes out of the policy work that you are focused on at the moment, it would be fantastic to get to a position where local authorities did have to provide that data through to the Environment Agency. If the Environment Agency registered it, and it was publicly available and available to insurers, that would be a huge step forward in terms of

improving information as well as providing a behavioural disincentive to developers who think that they can build on a floodplain. There might be a bit of fuss about it at the time in a few local papers and so on but, at the end of the day, everyone will forget about it. We have to move away from that sort of position and so I very much welcome anything which improved the focus on that area.

Chair: We have noted that.

Huw Evans: Since it is not there, we unfortunately cannot give a definitive answer to that question.

Chair: Thank you very much, gentlemen, for the very good evidence. It will form part of our report.