

Flood insurance, Flood Re and the recent floods

Submission by the Council of Mortgage Lenders

Introduction

1. At its evidence session on 11 March, the Committee will consider the response of the insurance industry to the recent winter floods and the impact of those floods on the Flood Re proposals, for which the Water Bill is currently paving the way.
2. Ahead of that session, we are providing this briefing to set out our headline concerns principally about the extent of the exclusions from the Flood Re scheme, which will generally not accept households where the insurance is arranged commercially. In effect, this means most leasehold and private rented homes would be excluded for buildings cover under Flood Re.
3. The CML is the representative trade body for the UK residential mortgage lending industry. Our 117 members currently hold around 95% of the assets of the UK mortgage market. In addition to lending for home ownership, the CML's members also offer buy-to-let mortgages to support the private rental market.

The issues; CML position

4. Having buildings insurance covering normal insured perils (including flood) is a requirement of all mortgages. This is to protect both the borrower and the lender in the event that an insured event happens to a mortgaged property. If insurance is completely unavailable for a property then a consumer would not be able to buy that property with a mortgage.
5. The CML supports the policy objective of ensuring that household buildings insurance with flood cover continues to be available and affordable. This would allow the housing and mortgage markets to continue to work in flood risk areas.
6. The Flood Re model appears to be a sensible way forward, provided that any exclusions from the scheme are not cast too widely.
7. There are key aspects of the detail of Flood Re that should be further developed in the Water Bill. Crucially, "household premises" is not yet defined. This is causing concern about types of properties which will be included and excluded from the scheme.
8. Last summer's Memorandum of Understanding, and the subsequent DEFRA consultation and impact assessment all refer to Flood Re as protecting eligible households and householders, without definition.
9. It has recently become clear that the scheme will exclude leasehold properties and private rented properties because they are usually insured on commercial contracts. We think this is inconsistent with the stated aim of protecting households and householders.
10. The reasonable person in the street would not see and probably be unaware of this technical distinction, which could limit Flood Re's exposure to all but the simplest and easily identifiable domestic insurance contracts. Households where the insurance is commercially arranged would be left to fend for themselves.
11. Given the recent flooding, we do not know how commercial insurers will react, in terms of their pricing going forward. We also do not know what their appetite will be in future for insuring leasehold and private rented homes.
12. It is possible that commercial insurance prices could rise, or the insurance might be less available. It is not unforeseeable that increased costs could be passed on to leaseholders and tenants.

13. This would result in an unfair situation where leaseholders and private landlords would, in effect, face full market pricing as soon as Flood Re is introduced, rather than a gradual move to risk-reflective pricing via Flood Re, in around 25 years time.

14. To address this, we believe government should urgently consider:

- Including leasehold and private rented homes in Flood Re on the basis that they are, in anyone's mind, household premises where Council Tax is payable.
- If this is not feasible in the time available (noting that it is intended to introduce Flood Re from next summer), then government should provide transitional protection on price and availability of commercial insurance for homes which would be excluded from Flood Re, so as to ensure there is a level playing field for all household tenures in accessing the buildings insurance they need.
- We would also like to see government and the insurance industry monitor the impacts of exclusion from Flood Re on commercially insured homes, with an evaluation of and report on impacts 2 years after Flood Re implementation.

15. In the Lords Committee debates on the flood insurance clauses in the Water Bill, Lord De Mauley said the government recognised "that the leasehold sector presents a more complex situation, where the contents policy is classified as domestic but the buildings policy could be classified as either commercial or domestic and could cover multiple dwellings." He went on to say that government would consider the issue in more detail and provide an update at report stage. We would like to see government take the opportunity of this update on report to signal a positive commitment to protect leasehold and private rented households.

16. With the Water Bill clauses on insurance due to be debated again in the near future, the recent floods are a timely reminder that Government and the insurance industry need to get the detail right, so that all eligible households are protected, regardless of tenure, as was intended.

17. We believe that there should be careful consideration of the impact on households or excluding leasehold and private rented properties from the scheme.

18. Much of the recent debate in this area has included calls for evidence of the problem for commercially insured households which would be excluded. We point out that because these properties still enjoy protections on insurance availability by virtue of the ongoing Statement of Principles, there can be no empirical evidence of a problem. Regrettably, evidence will begin to emerge only after the partial solution of Flood Re has been implemented and the commercial insurance market has had time to react to recent flood events.

Contact

19. Please contact CML if you would like to discuss this submission further.

10 March, 2014