



Flood of Options



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A study conducted by the Institute for Catastrophic Loss Reduction (ICLR) and Swiss Re concludes overland flood is insurable for Canadian homeowners.

Insurance companies have provided coverage against fire and other perils in Canada for more than 200 years, yet consistently they have chosen not to provide flood insurance to homeowners. Businesses in Canada buy flood coverage. Homeowners have the option of buying flood insurance in the United States, Japan, Germany, the United Kingdom and France. What is needed to make flood insurable for Canadian homeowners?

Flooding accounts for almost half of the disasters in Canada. Insurance is available for other perils in Canada — earthquake, tornado, hurricane, wildfire, winter storms, lightning and hail — but not overland flood. Relief programs offered by government agencies and charitable groups reduce the hardship for flood victims, but funding to support immediate, basic needs is not insurance.



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Joint research by the Institute for Catastrophic Loss Reduction (ICLR) and Swiss Re assessed flood insurance models operating around the world to identify what would be needed to make flood insurable for Canadian homeowners. Our proposal would be unique to Canada, while largely adopting the system presently in place in the United Kingdom. The essence of the proposal involves forging a partnership. Governments provide mapping, flood defense and restricted development in flood zones. The insurance industry commits to include flood coverage for all property owners that purchase fire and theft insurance, assuming the property is located outside of the zone where the government should not permit development.

Private insurers are responsible for the business of insurance, such as paying flood damage losses and accurate pricing of this risk. Government is responsible for providing the information that insurers, homeowners and local governments need to manage the risk of flooding. In addition, the government is responsible for risks associated with allowing some homes to locate in zones of high risk.

This proposal will be attractive to insurers to the extent they are successful in negotiating

commitments from the government that provide confidence that maps, defense structures and development will be appropriately managed, and insurers are free to ensure adequate prices for the coverage provided.

This proposal will be attractive for governments when flood insurance becomes available for most Canadian homeowners.

Insurance companies have been providing bundled flood insurance coverage to homeowners in the United Kingdom for almost 50 years. The ICLR and Swiss Re believe many aspects of this model may be effective in Canada. We believe governments in Canada should provide stronger commitments to insurers about mapping, defense and development. Also, there need to be strong incentives to involve homeowners directly in flood risk reduction. In particular, homeowners failing to take certain protective actions should pay accordingly through deductibles and appropriate rates.

OVERLAND FLOOD COVERAGE MODELS

Our research identified many models for providing flood insurance.

United States

In the United States, public officials determine prices and coverage; homeowners are offered basic flood coverage as an option that can be added to fire and theft coverage. Flood damage claims paid in the United States have exceeded revenues by almost \$20 billion; despite this public subsidy, the vast majority of homeowners choose not to purchase flood coverage. We are not aware of any country that has copied the troubled and ever changing American flood insurance program, nor should Canada.

Germany

In Germany, private insurance companies offer coverage to homeowners as an optional addition to their fire and theft coverage. Generally, pricing has been sufficient to cover claims over the longer term. However, most homeown-

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ers do not choose to purchase flood coverage. Poor take-up presents serious challenges for the government and insurers following major flood events. Flood relief paid to homeowners who do not buy insurance further erodes efforts by private insurers to sell coverage.

France

In France, the government has established a program covering losses that

result from flood, earthquake and a number of other natural hazards. All homeowners purchasing fire and theft insurance are required to participate. The price of coverage is set by the government and is uniform across the country, so it does not reflect the actual risk of loss. Political processes are used to determine specific events that trigger the payment of claims. The program has been successful in securing broad participation, but this model provides no incentives to property owners to participate in damage risk reduction: it transfers risk, but does not also reduce the risk of damage.

A number of other flood insurance models are in place around the world. All involve an active and continuing relationship between the insurance industry and government agencies responsible for flood risk reduction.

CANADIAN CHALLENGES

One special challenge in the Canadian environment is the many different government agencies involved in flood management. Issues like mapping, flood defense and zoning are provincial responsibilities or municipal concerns under provincial guidance, so the Canadian insurance industry would need to establish several partnerships to bring flood insurance to homeowners across Canada.

The federal government withdrew from the Flood Damage Reduction Program more than 15 years ago; since then, it has had little role in flood management. The state of flood mapping and defense differs from province to province. Our research focused on the four provinces with the largest populations — 85% of Canadian homes are located in Ontario, Quebec, British Columbia and Alberta. In many respects, Quebec has sustained the strongest commitment to flood risk reduction, perhaps presenting a jurisdiction where the insurance industry could first look to explore the idea of a partnership model in Canada.

There would be a number of potential benefits for Canada's insurers if flood

coverage is introduced for homeowners following the partnership model identified by the ICLR and Swiss Re. In particular, the provision of flood coverage should:

- eliminate a significant misunderstanding (70% of Canadian homeowners currently believe their insurance policy includes flood cover);



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- remove the need for complex policy wordings detailing coverage available for sewer back-up and other water damage, excluding overland flooding;
- engage consumers in loss prevention, potentially through the introduction of significant deductibles for homeowners that fail to protect their property;
- launch a partnership with government that clarifies the role of insurance and the role of government in disaster risk

management, particularly the financial role;

- extend coverage to include the natural peril most commonly experienced by Canadians, yet is not currently part of basic homeowners coverage;
- enhance the insurance industry's capacity to continue to provide commercial flood coverage by securing mapping, flood defense and zoning information;
- bring Canadian homeowner coverage more in line with property insurance coverage available in the other major insurance markets around the world;
- anticipate the needs of consumers, since climate change is increasingly expected to influence the future coverage requirements of homeowners;
- clarify that governments are responsible for helping property owners allowed to locate in zones of high risk, as this risk is uninsurable; and
- expand the product offering by insurers for consumers.

ICLR and Swiss Re research finds it is possible for flood to become insurable for homeowners in Canada. We need to establish a partnership involving insurers, governments and homeowners jointly working to manage the risk of flood damage.

The next step toward making flood an insurable peril for Canadian homeowners would involve debate among insurance companies to determine if there is a consensus to address this issue. Should the insurance industry choose to take this issue to governments, we believe the initial discussion would focus on one or two provinces. It will likely take many years before a national flood insurance program could be secured. The ICLR and Swiss Re are available to support this effort, and we have set out our joint research in the publication *Making Flood Insurable for Canadian Homeowners*.

Canada's insurers must immediately address issues that include restoring profitability in auto and property coverages, insurance to value and increasing water damage claims. Nevertheless, this appears to be an excellent time to launch a discussion about flood insurance.

It is possible for flood to become insurable for Canadian homeowners. ≡