Response of The Netherlands to EC Green Paper on the insurance of natural and man-made disasters

1. Natural disasters

Impediments for disaster insurance

The Netherlands supports an enlargement of the possibilities for citizens and private enterprises to mitigate the negative financial and economic impact of natural disasters. Uncertainty about this impact could restrain economic development, as is also put forward in the green paper. In an ideal situation natural disaster insurance would be available for everybody, preferably offered by multiple providers. When the premium of this insurance reflects real risk moral hazard can be reduced (e.g. by encouraging citizens and private enterprises to incorporate this aspect in their assessment to settle at a certain location or to take necessary precautionary measures to prevent or limit damage.) Moreover, the possibility for citizens and private enterprises to choose for an insurance voluntarily, will force providers to limit the premium amount to a reasonable level. It is evident that this ideal situation is not established by itself. Various impediments, which discourage insurers and reinsurers to offer a (sufficient) coverage capacity or make consumers and private enterprises renounce from an insurance, are mentioned in the green paper. This is mainly related to (1) premium setting and (2) too great uncertainty and a lack of knowledge about the nature of the risks involved.

1. Natural disaster insurances in high risk areas can often only be offered at a prohibitively high premium. For this reason many insurers will not consider it expedient to market such products. Leveling the insurance premiums (i.e. lowering them in areas with a high risk exposure and increasing them in areas with a low risk of natural disasters) could have the effect that the insurance is not purchased anymore in the latter areas. The extent in which these dilemmas are present is dependent on the concentration level of risks in certain areas and the level of preventive measures taken by the public authorities. These factors vary throughout member states. A study on the penetration level of disaster insurances with the EU may therefore not provide univocal answers.

2. The uncertainty about the risk that a disaster occurs and the damage resulting from it, may prevent insurers from offering natural disaster insurances (at reasonable premiums). In addition this uncertainty may also make it impossible for citizens and private enterprises to assess whether an insurance is necessary. This problem could be mitigated if parties are better informed about the nature and the consequences of the risks they run. The Netherlands has not received any indications that specific public measures, besides the information systems of insurers, are desirable to improve this information. Flooding risks are currently sufficiently mapped. A method for that is the application of flooding risk and danger maps which are developed within the framework of EU-ROR. In the Netherlands this is supplemented with information from the safety regions. The EU-directive INSPIRE will make all public spatial data available on European level. This data can be used to evaluate risks. Thus, for this purpose European action is already accommodated. The regional differences in Europe are considerable, so the public assessment and criteria to describe and measure risks vary in each country. The Netherlands holds the opinion that these differences should be taken into account in case risk analysis en models are exchanged.

The state as insurer

Despite the above mentioned factors that may impede the development of natural disaster insurances on the market, it is desirable that (the implementation of) initiatives is taken in hand by the insurance branch itself. The Netherlands agrees with the green paper that a bigger involvement of the state would also increase the moral hazard problem. Not only would private persons find less necessity to take preventive measures, but also insurers would be less inclined to check if a negligent policy holder should bear (a part of) the loss himself, if a part of the financial risk is on the side of the state. For this reason the Netherlands is in principle not an supporter of measures which give the state wholly or partly the role of (re)insurer or compensation body. The Netherlands does have an Act on the compensation of loss by disasters, but this act does not contain an obligation for the state to compensate citizens (fully) for their loss. The specific rights which citizens and private enterprises can claim, are laid down in a more detailed governmental decision. The Netherlands considers it an omission that this option, which member states can easily introduce themselves, is not mentioned in the green paper. Naturally insurers are free to expand
the coverage facilities related to natural disasters by means of pooling and reinsurance constructions.

Compulsory insurances

A legal obligation for citizens and private enterprises to purchase a national disaster insurance is also not a measure which the Netherlands supports. Not only would this remove the pressure on insurers to hold premium on a market-based level, particularly in a market with a limited number of competitors, but citizens could also put forward justified objections against such fixed charges, certainly if the premiums are insufficiently diversified to risks, which gives them the nature of a solidarity levy. Moreover, it is not unlikely that the random loss by natural disasters and costs related to the uncertainty about the question if and in which degree of gravity these disasters will occur, are structurally lower for citizens and private enterprises than the fixed charges in order to remove this risk. The same considerations would apply to a legal obligation for insurers to bundle a natural disaster insurance with insurances which are essential for citizens and private enterprises, like fire and theft insurances. Since this would come down to an obligation to insure oneself, the Netherlands does not support this approach. Insurers are in principle free to increase the degree of penetration of natural disaster insurances by product bundling. As the freedom of choice of consumers is limited (with or without arrangements between insurers) and the charges for citizens and private enterprises increase, the question will rise if such bundling is admissible. Instead of an obligation member states could consider to provide a subsidy on a national level, notably in case the member state otherwise expects to pay out much higher random compensations. With a subsidy that insurance could become much more affordable. This is the case in the Netherlands with agricultural loss caused by extreme weather conditions.

Insurance conditions

The terms and conditions under which insurances are provided, could co-determine the success of a product. The green paper mentions several possibilities which the insurers could consider, like price setting on the basis of risks, fixed premiums, long-term insurance contracts, reducible amounts, policy excess arrangements and co-insurance. Which of these instruments is most successful in the sense that the degree of penetration of insurances is encouraged and moral hazard discouraged, is a question insurers should answer themselves, probably on the basis of trial and error. In the Netherlands we have too little experience with disaster insurances to make statements about this at this point in time.

2. Manmade disasters

Impediments for manmade disaster insurances

The Netherlands supports an expansion of the possibilities (and where applicable of the obligation) for industrial operators to acquire adequate liability risk insurance for specific risks which result from their economic activities. In this case the relation between the different interests is different from the insurability of natural disaster as discussed in the previous chapter. The risks and disasters involved are a consequence of a conscious choice to engage in risky (economic) activities, but the effects are also experienced by third parties. Insurances are not only in the interest of potentially injured parties, but the premium costs are also an internalization of the external costs connected to these activities.

Citizens and private enterprises usually do not have a specific insurance for the loss they suffer from an industrial incident at a nearby located installation. Related to citizens their health insurance and building insurance would usually cover a part of the loss. Citizens and private enterprise also dispose of less possibilities to prevent this loss, unlike the risk of natural disasters. For this reason it is mostly the operator who has (compulsory or not) taken out an insurance. An impediment for the insurability of these industrial risks is that it concerns mostly disaster scenarios which occur so rarely and unpredictable that is impossible to determine what kind of insurance (cover) is adequate. This introduces the risks of being over- or underinsured. Furthermore the amount insurers can provide coverage for will be insufficient in the case of big industrial disasters. Certainly if it concerns important activities for the national economy the public interest is especially served if the concerned activities are allowed under strict security regulation and adequate supervision.
The state as insurer

Taking into account the limited insurance capacity of the market, the question will soon rise whether involvement of the state is desirable. In the event of an industrial accident, the state might very well (also) be held responsible, particularly when she permitted, authorized and/or supervised the relevant industrial activities. This could ultimately result in a (moral or legal) obligation for the state to compensate the damage incurred by citizens or private enterprises as a result of the accident. In The Netherlands, the aforementioned Act on the compensation of loss can be made applicable in these situations. To mitigate the risk on this kind of incidental costs, it is possible to increase the risk absorption capacity of the private sector. This could be done by the state as (re-)insurer or participant in an insurance pool. Subsequently, for this role the state could charge industrial operators a premium (in line with the prevailing market).

The Netherlands, however, is not in favour of adopting such schemes on a large scale. In order to maintain the credibility of insurance programmes, government should not guarantee excessive sums of money. Furthermore, it is preferable that the state maintains some room for manoeuvre to act pragmatically, should for instance occur multiple disasters in a short period of time. Financial obligations that are fixed in advance, may limit the room for manoeuvre and offer little guarantees to citizens in need of compensation, while a willing government may be presumed to do its utmost in order to compensate citizens in the event of an accident. With regard to insurance against nuclear accidents, The Dutch state acts as insurer in addition to the insurance coverage offered by private insurers (united in a national insurance pool). It should be noted that this was principally done to fulfil treaty-obligations and in response to the Chernobyl-accident.

Subsequently, The Netherlands prefers to accommodate market initiatives for insuring manmade disasters and prefers to refrain from state involvement as much as possible. Nonetheless, governments could compel industrial operators with high risk activities to maximise their insurance coverage on the private insurance market by introducing strict liability schemes or even an obligation for industrial operators to acquire adequate liability risk insurance. This could at the same time stimulate the insurance market to enlarge its insurance capacity by using insurance pools and re-insurers. Proof that the aforementioned strategy works, is provided by the fact that the insurance capacity of the Dutch insurance pool for nuclear accidents in The Netherlands has tripled as of 1 January 2013 from €340 million to €1,2 billion. Additionally, Dutch offshore operators have been able to find adequate liability insurance as well.

3. Other subjects

The green paper also raises the question whether member states think there is a need to harmonise pre-contractual and contractual information requirements for non-life insurances. The Netherlands is not convinced of the necessity of such measure and notes that this subject goes beyond the scope of the green paper on the insurance of natural and manmade disasters. The Netherlands does not in this context want to comment on the desirability of harmonising pre-contractual and contractual information which could have consequences for the entire insurance market. A discussion on this issue should take place in the appropriate context, like the revision of the Insurance Mediation Directive (IMD2).

4. Conclusion

In sum, The Netherlands is not in favour of (new) European legislative measures to expand the availability and coverage of disaster insurances (natural and manmade). We believe the necessity of such measures is not adequately established and we feel the disadvantages of the measures explored in the green paper are larger than the potential advantages. The support for and the costs of an disaster insurance are – as we have explained in the paragraphs above – dependent on multiple factors like the concentration of risk areas within a member state, the amount and quality of the preventive measures taken by the member state and the nature of the risks involved. Additionally, a member state with a mature insurance market might be more inclined to trust on private initiative to provide insurance of natural and manmade disasters. The preconditions vary widely among member states. Therefore, the Netherlands believes it is not necessary and not in line with the principle of subsidiarity to take measures on a European level. Any measure taken by the European Commission on this issue should therefore be subject to close scrutiny and requires careful consideration.
The Netherlands believes that an adequate solution for the limited availability and coverage of disaster insurances, can be found in maintaining and accommodating market conditions that provide sufficient opportunity for developing and deploying market initiatives. Our observation of the Dutch disaster insurance market indicates that this approach is gradually yielding results. However, should the development of the market for disaster insurances be absent, the Netherlands believes a pragmatic approach is preferable in order to adequately mitigate the financial and economic consequences of disasters and incidents. The Dutch Act on the compensation of loss by disasters is an example of an instrument that fits this approach.