

**Mr. Thierry
Masquelier**
*Caisse Centrale
de Reassurances*



The French “CAT NAT” System: The Experience of the Last Fifteen Years

Introduction

France is obviously exposed to natural disasters, such as floods, storms, heavy snow, avalanches, landslides. Some areas of France, mainly the southeast are subject to earthquakes. Volcanic eruptions and hurricanes may be devastating in overseas departments. Of course, these natural disasters may impact heavily not only on individuals but also on properties, goods and more broadly on economic activities.

French public authorities are concerned about this both in terms of prevention and where and when a disaster occurs, in terms of contingency plans for victims. Several procedures exist which enable mobilizing public services, state funds and local community funds to prevent natural disasters and then to rescue victims.

Yet, since 1982, the compensation of victims of a natural disaster occurring in France takes place mainly through insurance covers with a combination of private and public initiative.

I will try to explain how this combination has been working for more than fifteen years in France and how it tries to be a compromise between public goals such as extensive protection of the individuals, solidarity between citizens and private objectives such as commercial efficiency, balance of the profit and loss account, and so on...

Obviously climate, geology and geography are different in each country. More importantly, the level of economic development, the cultural wish of each and every citizen to pay an insurance premium and/or to assume a part of the financial burden of a natural disaster are different. Specific solutions are to be found in each country. The system which has been working, apparently with success, in

France, would probably not be an effective solution in a different economical, political, geographical environment. But maybe some ideas could arise from this experience.

What is the French System? How does it work?

It was created in 1982 by law and has been in operation since that time without significant changes.

It is based on a compulsory clause included in each and every insurance contract against any kind of damages. It is not a compulsory insurance. Nobody is compelled to buy an insurance. But as soon as a company or an individual buys an insurance against fire, water damages, theft or whatever to protect his properties, his goods or his belongings, such goods, properties or belongings are protected against natural disasters in exactly the same conditions as if the main peril covered by the insurance policy occurs. The only minor difference is that the self-retention of the insured, the “franchise”, could be slightly different, generally lower in case of a natural disaster.

As far as industrial insurance is concerned, the coverage against natural disasters is extended to the loss of profit.

In France, almost all companies, being large or small, are insured against fire and more than 90 % of the individuals, being owner or tenant, protect their home with an insurance policy. Most of the cars are similarly protected against damages or theft. So, if not all, at least a very large share of the French citizens and of the economic agents are insured against natural disasters through the scheme. That was not the case in 1982. The natural disaster scheme undoubtedly played a role in the de-

velopment of insurance in France specially for homeowner insurance, mainly through the importance given by mass-medias to the consequences of a natural disaster and, therefore, to the usefulness of being properly protected by an insurance contract.

When an event occurs, the State will determine if this event is or is not a natural disaster and what is its geographical spread. This could come as a surprise to you that such a decision involving private insurance contracts would be taken by the State, actually the French Ministers of Finance and of Home Affairs. One could obviously fear some kind of political deviation. But this system has proved over the last 15 years, to be a very efficient mean, in practical terms, to discriminate between "usual events" and "natural disasters", for instance to discriminate between a flood which occurs every ten years or more, and "rising waters" or a river in spate which happens every second or third year.

In practical terms, any natural event whose intensity happens only once a decade or less would be considered as a natural disaster. Any natural event of such intensity that it occurs more frequently than once a decade at a given location, would not be considered as a natural disaster and would not be covered, at least under the compulsory clause, by the insurance policy

When a natural disaster did occur, the compensation of the losses is done by the insurers according to the insurance contract exactly as if the property was damaged by fire or otherwise. This way of compensation has proved, by far, more efficient in terms of delay and of fairness than any kind of compensation through public procedures.

Insurers are obviously better equipped than public servants to assess the loss, they generally have or send specialists in the devastated area, they make advance payments, they can also reach an agreement with the insured on the final cost of a loss more easily than a public servant complying to public procedures.

The victims are, generally speaking, fully compensated for their loss depending on the conditions of their insurance contract as opposed to compensation through public procedures which usually leave the victim bear a share of the loss.

This compulsory clause included in the insurance contract is obviously not free for the insured. The natural disaster premium is, generally speaking, 12 % of the global premium of the contract. This rate, 12 %, is the rate which gives, in France and derived from our experience, a long-term balance between premiums and losses.

A key point in the French system, is probably that the rate, whatever its level, is the same for each and every policy irrespective of the actual exposure of the insured to natural disasters. There could be exceptions to this rule but they are very few.

On one hand, this is a strong element of solidarity between citizens. The citizens living in comparatively safe areas will through the payment of insurance premium contribute to the protection of the others living in more exposed areas. On the other hand, this is a guarantee that nobody will be denied insurance or will have to pay an excessively expensive insurance premium because his exposure to natural disasters happens to be high.

The insurance companies usually reinsure part of their natural disaster exposure with reinsurers. They are not compelled to do so and some (very few I must say) do not. They may reinsure themselves either on the open market or with Caisse Centrale de Reassurance.

Caisse Centrale de Reassurance (CCR) is a stock company, is run exactly as a private company with private procedures and acts, for a large part of its activity, as a professional reinsurer outside of the scope of this natural disaster scheme. It is still owned by the French State but is on the list of companies to be privatized.

Acting as a reinsurer in the frame of the French natural disaster scheme, CCR benefits from a financial guarantee given by the State. That means that in case of an exceptionally large natural disaster, CCR could not be bankrupt due to such an event. Obviously, CCR pays an annual premium for this financial guarantee, which works exactly like a retrocession agreement.

I must add that this guarantee has been free of any kind of loss over the last fifteen years, with the exception of last year when we expe-

rienced a large flood in the South of France along the river Aude. All the natural disasters which did occur in France before last year, had been fully compensated by the insurers and CCR without any involvement of the State guarantee.

Such a guarantee is obviously crucial to confer to the system its long-term credibility.

What lessons could be derived from such an experience of 15 years ?

Undoubtedly, the system is globally well accepted by all the players concerned. The insured consider it natural, even obvious, to be compensated quickly and professionally through their insurance policy when a natural disaster happens.

Nobody is questioning the fact that natural catastrophes are covered through a compulsory clause in an insurance contract.

In the eyes of the government, one obvious advantage of the system is that natural catastrophes do not impact (or impact significantly less) public resources (with the exception of very large but infrequent natural catastrophes through the financial guarantee given to CCR) and that for “ordinary natural catastrophes”, claims and complaints are received and dealt with by insurers rather than public officers.

Additionally, the solidarity between citizens due to the uniformity of rate is considered a small but not insignificant element of being member of the French national community.

In the eyes of the insurers active in France, a significant premium income (approximately 750 million Euros) derives from this natural catastrophe scheme and, up to now, even if a loss is always possible, globally over fifteen years, a rather regular profit (partially considered as equalization reserve) arose from this class of business.

Additionally, the French insurers are globally in favor of such a scheme even if it is not “pure insurance”, even if there is some kind of public involvement incorporated in it rather than to see natural perils exclusively covered through public procedures.

The opponents to the system are rather to find on the “public safety” or “prevention” side. Undoubtedly, people in charge of pre-

vention policies against natural catastrophes see Cat Nat insurance as an excessive protection of the insured. In their eyes, the citizens or the local public officers or political executives loose, to a certain extent, their incentive to take the necessary measures against natural catastrophes when they know that they will be compensated, if not totally, at least to a large extent when a Cat Nat occurs.

It is foreseeable that the compulsory clause could be in the future slightly modified to reduce compensation when there is a repetition of losses with no measures of prevention taken. A first step in that direction will be made as of 1/1/2001 when the retention of the insured will be higher and higher if a peril did occur several times in the same town or village with no local plan in elaboration or in force to prevent such peril.

It is not unthinkable that, sometime in the future, the rates could be somehow modulated, rather than completely uniform, according to the experience of the risk in order to encourage the insured to take prevention measures.

Fundamentally, the French Cat Nat system is based on some kind of equilibrium between a public and global approach of natural perils on one hand and private techniques and insurance procedures on the other hand. Like any equilibrium, the balance between these two philosophies (which could be contradictory on some aspects) is bound to be flexible when the surrounding world is changing.

Our experience in France seems to indicate that the insurance concepts will probably, slowly but regularly, take a larger and larger place in the French Natural Catastrophes insurance system.