Norsk Naturskadepool
Norwegian Natural Perils Pool

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Accounting of New Regulations for the Norwegian Natural Perils Pool

1. Background

In connection with the amendment of the Norwegian Natural Perils Insurance Act regarding the establishment of a common natural perils capital fund in the Norwegian Natural Perils Pool, a new regulation on natural perils insurance in Norway was adopted. The new law and regulation on natural perils insurance will come into effect on 1 January 2025. This document contains a **recommended solution** for how the changes should affect the members of the pool's accounting of natural perils related to the scheme. Discounting of reserves is not considered in this recommendation.

The principle is defined in the Parliamentary Proposition, pages 25-26:
"The proposed legislation on the establishment of a common natural perils capital in the Norwegian Natural Perils Pool specifically means that in **claims years with a positive balance**, a member of the pool shall transfer its share of the balance to the pool's natural perils capital. In **claims years with a negative balance**, the member's share of the negative balance will be covered by the pool's natural perils capital."

The right to settle a claims year expires after ten years, according to Section 33, first paragraph of the Norwegian Natural Perils Insurance Regulation. Since the balance of the claims year will only be known ten years after the end of the claims year, and a cash settlement is to be made every year based on a preliminary calculation of the claims year's balance, an interpretation of the text in the law is required for this to be handled in ongoing accounting. The balance for each year will be defined according to Section 39 of the Norwegian Natural Perils Insurance Regulation.

2. Claim Year 2024 and Earlier

According to Section 50, fifth paragraph of the Norwegian Natural Perils Insurance Regulation, it is clear that claims years before 2025 shall be accounted for according to the rules in the regulation dated December 21, 1979, no. 3420, concerning instructions for the Norwegian Natural Perils Pool. In short, this means that:

Any liquidation gains or losses, i.e. change in previous claims years' paid claims and reserves, is recorded as usual in the income statement and will increase or decrease the natural perils capital.

The natural perils capital reserved according to the regulation for the Norwegian Natural Perils Pool belongs to the member company and should only be used to cover future natural perils in Norway, according to Section 41 of the Norwegian Natural Perils Insurance Regulation. See Section 3.1 for the use of already reserved natural perils capital for claims years 2025 and beyond.

3. Claims Year 2025 and Beyond

A new account for natural perils capital should be established for claims years from 2025 and onward, to differentiate them from the old system. No additional natural perils capital can be built up by the members for claims year 2025 and beyond. The balance must at all times be negative in the event of a loss, or zero in the event of a surplus for the claims year. It is necessary to book fund changes separately for each claims year.

For a period, until the central fund has reached a size of NOK 4 billion, there will be a distinction between member companies that have natural perils capital in their own books and those that have not.

In brief, this means that during the transition period, insurance companies with positive natural perils capital must use this to cover their share of the annual deficit, while companies without natural perils capital will have their share of the deficit covered by the pool’s central fund.

Additionally, according to the Norwegian Natural Perils Insurance Act, section 4, third paragraph, if the natural perils capital of the pool is not sufficient to fully or partially cover the deficit, the member must cover their share of the remaining deficit.

3.1 Companies with Booked Natural Perils Capital in Their Own Accounts

Until the pool's natural perils capital reaches a size of NOK 4 billion, members who have booked natural perils capital in their own accounts must cover the deficit from their own capital before they can claim the deficit to be covered by the pool’s fund, as per section 4, fourth paragraph of the Norwegian Natural Perils Insurance Act.

Any natural perils capital remaining in the company when the transition period ends belong to the company and must only be used for future natural perils, according to section 41 of the Norwegian Natural Perils Insurance Regulation. If the pool’s natural perils capital falls below NOK 3 billion within ten years after the end of the claims year in which it reached NOK 4 billion, members with booked natural perils capital will again have to cover the deficit themselves, as per section 4, fourth paragraph of the Norwegian Natural Perils Insurance Act.

3.1.1 Current Claims Year

If the balance for the claims year at the balance sheet date is positive, the company will record an expense (debit) for paid claims equal to the surplus and simultaneously record the same amount (credit) against an interim account. When the invoice from the Norwegian Natural Perils Pool is received, it will correspond to the amount on the interim account, which will then be settled against the bank without any income statement effect.

If the claims year’s balance is negative, no further entries are made in the income statement, but the natural perils capital is adjusted downwards in the same way as for claims years 2024 and earlier.

3.1.2 Different Scenarios in the Current Calendar Year for Previous Claims Years

From the calendar year 2026 and beyond, it will be necessary to distinguish between different scenarios for previous claims years. The following amounts are defined (note that a simplification has been made so that Balance2 is only affected by the liquidation result):

Balance1 = The balance at the start of the year for the claims year.
Balance2 = The balance of the claims year at the balance sheet date.
Balance2 = Balance1 + liquidation result (+ is income)

1a) The balance of the claims year is positive at the beginning of the year (Balance1) and there is a liquidation gain. The balance at the balance sheet date (Balance2) is still positive.

The liquidation gain is offset against paid claims as for the current year, and the same amount is credited to the interim account.

Paid claims = Balance2 – Balance1 (expense)
No entry against the natural perils capital.

1b) The balance of the claims year is positive at the beginning of the year (Balance1) and there is a liquidation loss. The balance at the balance sheet date (Balance2) is still positive.

The liquidation loss is offset against paid claims, and a debit is recorded against the interim account, as the company needs to receive a refund from the pool.

Paid claims = Balance2 – Balance1 (income)
No entry against the natural perils capital.

1c) The balance of the claims year is positive at the beginning of the year (Balance1) and there is a liquidation loss. The balance at the balance sheet date (Balance2) is now negative.

The liquidation loss is adjusted against paid claims until the claims year's balance reaches zero, while the remainder of the liquidation loss must be covered by the company's natural perils capital.

Paid claims = -Balance2 (income)
Change in natural perils capital = Balance2 (negative)

2a) The balance of the claims year is negative at the beginning of the year (Balance1) and there is a liquidation gain. The balance at the balance sheet date (Balance2) is still negative after the liquidation gain.

No entry is made in the result, as the balance of the claims year is still negative. The natural perils capital is increased by the liquidation gain.

Paid claims = 0
Change in natural perils capital = Balance2 – Balance1 (positive)

2b) The balance of the claims year is negative at the beginning of the year (Balance1) and there is a liquidation gain. The balance at the balance sheet date (Balance2) is positive.

The portion of the liquidation gain that brings the balance to zero for the claims year is transferred to the natural perils capital, while the part that makes the balance positive is recorded as paid claims and against the interim account.

Paid claims = Balance2 (expense)
Change in natural perils capital = -Balance1 (positive)

2c) The balance of the claims year is negative (Balance1) and there is a liquidation loss. The balance at the balance sheet date (Balance2) is negative.

No further entry is made in the result, and the entire liquidation loss reduces the natural perils capital.

Paid claims = 0
Change in natural perils capital = Balance2 – Balance1

With this approach, the final result for each claims year will only depend on the final balance for each year, and not on how it was arrived at (i.e., whether the claims year was correctly estimated all along or if there were fluctuations).

3.1.3 Detailed Settling for Companies with Booked Natural Perils Capital in Their Own Accounts

Example

Company Y has booked natural perils capital. In 2025, there is a loss of NOK 5 million for the claims year. Since the central fund in the pool has not yet reached a size of NOK 4 billion, the loss of 5 million is charged to the company's own natural perils capital. In 2026, the company has a surplus of NOK 6 million for claims year 2026. Additionally, we have different scenarios for the development of claims year 2025 in calendar year 2026:

a) Further liquidation loss of -2 million, so the balance for claims year 2025 is now -7 million

	2025	2026	
2025	-5		The company's natural perils capital decreases by 5
2026	-2	6	The company's natural perils capital decreases by 2 and 6 is transferred to the pool
	-7	6	

No transfer to the pool is made for claims year 2025 as it is still negative (-7)

b) No change in the balance, the balance for claims year 2025 is still -5 million

	2025	2026	
2025	-5		The company's natural perils capital decreases by 5
2026	0	6	The company's natural perils capital is unchanged and 6 is transferred to the pool
	-5	6	

No transfer to the pool is made for claims year 2025 as it is still negative (-5)

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c) Liquidation gain of 3 million, so the balance for claims year 2025 is now -2 million

	2025	2026	
2025	-5		The company's natural perils capital decreases by 5
2026	3	6	The company's natural perils capital increases by 3 and 6 is transferred to the pool
	-2	6	

No transfer to the pool is made for claims year 2025 as it is still negative (-2)

d) Liquidation gain of 6 million, so the balance for claims year 2025 is now +1 million

	2025	2026	
2025	-5		The company's natural perils capital decreases by 5
2026	6	6	The company's natural perils capital increases by 6 and 7 is transferred to the pool
	1	6	

The balance for claims year 2025 is now positive (1) and the surplus of 1 is transferred to the pool.

3.1.4 Summary for Companies with Booked Natural Perils Capital in Their Own Accounts

For companies with booked natural perils capital (which do not have the deficit covered by the central fund until the fund reaches NOK 4 billion, or if the pool's natural perils capital falls below NOK 3 billion within ten years after reaching NOK 4 billion), this can be compactly written as follows:

In the result:
Paid claims = max(Balance2, 0) – max(Balance1, 0)

In the natural perils capital:
Fund change = min(Balance2, 0) – min(Balance1, 0)

The *cumulative* entry (sum of entries over all accounting years) for the claims year is thus:
Paid claims (to the central fund) = max(Balance2, 0)
Change in natural perils capital = min(Balance2, 0)

Thus, the surplus is paid to the central fund, and the deficit is charged to the member's natural perils capital. Cumulatively, a claims year will never be able to increase the natural perils capital.
These formulas will also apply for the current year if we set Balance1 = 0 for a new claims year. If a member runs out of natural perils capital during the year, this will require a modification of the setup.

3.2 Companies without Booked Natural Perils Capital in Their Own Accounts

3.2.1 Current Claims Year

If the balance for the claims year is positive at the balance sheet date, the company records an expense (debit) for paid claims equivalent to the surplus and simultaneously credits the same amount to an interim account. When the invoice from the Norwegian Natural Perils Pool is received, it will correspond to the amount in the interim account, which is then cleared against the bank without affecting the result.

If the balance for the claims year is negative, and assuming there are sufficient funds in the central fund to cover the deficit, the company records income (credit) for paid claims equivalent to the deficit and simultaneously debits the same amount to an interim account. When the payment from the Natural Perils Pool is received, it will correspond to the amount in the interim account, which is then cleared against the bank without affecting the result. If there are insufficient funds in the central fund, the member must cover their share of the remaining deficit, which will result in a loss being recorded in the income statement, reducing the company's equity.

3.2.2 Further Details on Settlement for Companies without Natural Perils Capital

Example

Company X does not have natural perils capital. In 2025, a profit of 5 million is recorded for the claims year, which is transferred to the pool's fund. If a loss occurs in 2025, the new scheme will start in 2026. Since there will be no fund available to cover the loss, any deficit in the scheme for 2025 will be charged to the company's equity. In 2026, the company incurs a loss of 6 million for claims year 2026. The following is the development of claims year 2025:

a) **Liquidation loss of -2 million, so the balance for claims year 2025 is now 3 million**
The loss in 2026 is added to the liquidation loss for 2025, resulting in a total loss of 8 million. 5 million is transferred from the fund, which is emptied, covering part of the loss. The remaining loss of 3 million is charged to the company's equity.

	2025	2026		
2025	5		5	Surplus: 5 is transferred to the pool
2026	-2	-6	-8	Deficit: 5 is transferred from the pool, and the company's equity decreases by 3.
	3	-6	**-3**	Deficit: the pool's fund is empty, and the rest of the loss must be covered by the company's equity.

b) **No change in balance, the balance for claims year 2025 is still 5 million**
The loss in 2026 is partially covered by the now emptied fund. 5 million is transferred from the pool, and the remaining loss of 1 million is charged to the company's equity.

	2025	2026		
2025	5		5	Surplus: 5 is transferred to the pool
2026	0	-6	-6	Deficit: 5 is transferred from the pool, and the company's equity decreases by 1.
	5	-6	**-1**	Deficit: the pool's fund is empty, and the rest of the loss must be covered by the company's equity.

c) **Liquidation gain of 3 million, so the balance for claims year 2025 is now 8 million**
The loss in 2026 is added to the liquidation gain for 2025, resulting in a total loss of 3 million, which is transferred from the fund, covering the entire loss. The fund now has 2 million left for covering future losses.

	2025	2026		
2025	5		5	Surplus: 5 is transferred to the pool
2026	3	-6	-3	Deficit: 3 is transferred from the pool
	8	-6	**2**	Surplus: the pool's fund now has 2 to cover deficits in the future

d) Liquidation gain of 6 million, so the balance for claims year 2025 is now 11 million

The loss in 2026 is covered by the liquidation gain for 2025, and no transfer to/from the fund occurs. The fund still has 5 million left to cover future losses.

	2025	2026		
2025	5		5	Surplus: 5 is transferred to the pool
2026	6	-6	0	The result is 0: No transfer from/to the pool is done
	11	-6	**5**	Surplus: the pool's fund still has 5 to cover deficits in the future

e) Liquidation gain of 8 million, so the balance for claims year 2025 is now 13 million

The loss in 2026 is added to the liquidation gain for 2025, resulting in a total profit of 2 million, which is transferred to the pool's fund. The fund now has 7 million to cover future losses.

	2025	2026		
2025	5		5	Surplus: 5 is transferred to the pool
2026	8	-6	2	Surplus: 2 is transferred to the pool
	13	-6	**7**	Surplus: the pool's fund now has 7 to cover deficits in the future

For companies both with and without natural perils capital, the principle is that the result should depend solely on the final balance for the claims year, not how this balance evolves along the way. Each claims year is treated on an account basis until it is fully settled after 10 years, and settlements are continuously carried out for up to 10 claims years in connection with transactions with the fund.

3.2.3 Summary for Companies without Booked Natural Perils Capital in Their Own Accounts

For companies without natural perils capital, the formula is simplified to:

Paid claims = Balance2 – Balance1

This assumes that there are always sufficient funds in the central fund to cover deficits, as surpluses and deficits are treated symmetrically in this case. If there are insufficient funds in the central fund, questions arise regarding the priority of claims, where the oldest claims years are given the highest priority in the case of liquidation losses.

4. Details on Compensation for Members' Administrative Costs

The Regulation on Natural Perils Insurance section 39 lists 9 different items that together define the balance for each claims year and determine whether there is a surplus or deficit. Item 1 is the earned premium income, which the companies know themselves. Items 2-8 are items that will be reflected in monthly settlements from the Norwegian Natural Perils Pool, while item 9 is "compensation for members' administrative expenses." In the same regulation, section 38 states that each member's administrative costs for each claims year are to be compensated with 0.005 per mille of the member's total fire insurance sums as of July 1st in the claims year.

There will be no actual cash flow from the Norwegian Natural Perils Pool to each company for administrative costs. The compensation for companies means, in practice, that this amount can be deducted from the calculation of profits or increase the deficit, thereby affecting equity.

Until July, the amount for the year will not be known, and it will be up to each company how to estimate the administrative costs for the year. For example, a formula can be used based on an estimated insurance sum for the year, or the forecast can be based on expired or earned premiums adjusted with the current rate.