

Key Questions to Ask in Designing a Pandemic Risk Insurance Program

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on Insurance

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Policy Objective: Establish a Risk Transfer Mechanism for Epidemic Infectious Disease

- Such a mechanism will enable businesses to:
 - Obtain loans at favorable rates
 - Address liability risk
 - Keep key personnel employed during shutdowns
- It will also serve larger social goals
 - Maintain payroll across workforce (not necessarily in a firm's narrow self-interest)
 - Dampen downward economic spiral

Two Approaches for Achieving This Objective

Government Assistance

- Payroll Protection Program (PPP)
- Liability shield with compensation for injured parties

Insurance Mechanism

- Business expense policies (including payroll)
- Liability policies
- Insurer policy underwriting and claim payment infrastructure

An Insurance Mechanism Has Both Benefits and Drawbacks

Benefits

- Sets benefits in advance
- Uses existing claims-paying infrastructure
- Leverages insurer expertise in risk mitigation
- Transfers some pandemic risk to the private sector

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Drawbacks

- Amount of risk insurers willing to take on appears small
- Potentially low take-up
- Difficulty determining appropriate rates
- Coverage litigation

Here, We Examine Six Key Questions to Ask in Designing a Pandemic Risk Insurance Program

1. How much risk should the private sector bear?
2. How much protection should the program provide?
3. Should the government charge a premium for the risk it bears?
4. Should business be required to purchase coverage?
5. Should the program be bifurcated by firm size?
6. Should workers compensation and general liability be included?

1. How Much Risk Should the Private Sector Bear?

Policy objective: Move some risk to private sector and give insurers incentives to carefully underwrite and adjust claims

Proposals	Private-Sector Risk
BCPP primary	No private-sector retention for primary program
PRIA	Insurers pay 5% of claims cost over a deductible up to cap (insurer exposure ~\$50B)
Chubb SME program	Insurers pay 5–6% up to industry cap (insurer exposure increases from \$30 to \$60B over 20 years)

1. How Much Risk Should the Private Sector Bear?

Policy objective: Move some risk to private sector and give insurers incentives to carefully underwrite and adjust claims

Considerations

- Insurer outlays modest in comparison to government outlays
- Skin in the game aligns insurer and government incentives in paying claims
- Trade off between larger private-sector role and insurer interest in participating in program

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2. How Much Protection Should Program Provide?

Policy objective: Provide protection that meaningfully reduces the risk

Proposals	Mandatory Offer
BCPP primary	Up to 80% of business expense up to 3 months (primary option)
PRIA	Coverage on same terms and conditions as BI policy; program cap \$750B
Chubb SME program	Up to 80% of business expense up to 3 months (\$20 million per month cap for large employers)

2. How Much Protection Should Program Provide?

Policy objective: Provide protection that meaningfully reduces the risk

Considerations

- Closures may last much longer than three months
- Pro-rating of claims payments once cap is reached magnifies uncertainty and generates policyholder dissatisfaction
- Option for how best to extend/augment benefits should be considered

Proposals	Mandatory Offer
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3. Should Government Charge Premium for Risk It Bears?

Policy objective: Impose program costs on those who benefit, reduce moral hazard, accumulate funds for future claims

Proposals	Government Premium
BCPP primary	Pricing designed to ensure widespread take-up and reduce moral hazard
PRIA	No charge for federal share; insurers charge to cover their share
Chubb SME program	No charge for federal share; insurers charge to cover their share

3. Should Government Charge Premium for Risk It Bears?

Policy objective: Impose program costs on those who benefit, reduce moral hazard, accumulate funds for future claims

Considerations

- Can't expect businesses to pay for social goal of payroll replacement for all employees
- Government benefits from limited downward economic spiral and reduced tax base
- Premium revenue may cover costs of smaller regional events
- Meaningful premiums provide opportunity for rate reductions for risk mitigation programs
- Should consider premiums that result in rates that businesses are willing to pay

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4. Should Businesses Be Required to Purchase Coverage?

Policy objective: Widespread take-up of pandemic risk insurance

Proposals	Mandatory Purchase
BCPP primary	No, but opt-out required
PRIA	No
Chubb SME program	No, but strong opt-out required

4. Should Businesses Be Required to Purchase Coverage?

Policy objective: Widespread take-up of pandemic risk insurance

Considerations

- Mandatory purchase is not popular
- A strong opt-out might help, but is withholding government assistance politically credible?
- Solution to high take-up may be attractive prices with perhaps the help of lenders
- An education campaign may also help
- Must balance low premiums with government cost

Proposals	Mandatory Purchase
BCPP primary	No, but opt-out required
PRIA	No
Chubb SME program	No, but strong opt-out required

5. Should Eligibility and Program Benefits Vary by Firm Size?

Policy objective: Target program benefits to firms that need them and take advantage of efficiencies to be gained by tailoring program to structure of market

Proposals	Variation in Program by Firm Size
BCPP primary	None
PRIA	None
Chubb	Separate programs for (1) firms with <500 employees and (2) firms with ≥ 500 employees

5. Should Eligibility and Program Benefits Vary by Firm Size?

Policy objective: Target program benefits to firms that need them and take advantage of efficiencies to be gained by tailoring program to structure of market

Considerations

- Large disparity between number of small and midsize vs. larger firms makes separate approaches for adjusting claims attractive
- Larger firms have more risk-management options and may prefer to tailor their strategy
- Lower subsidies may be warranted for larger firms

Proposals	Variation in Program by Firm Size
BCPP primary	None
PRIA	None
Chubb	Separate programs for (1) firms with <500 employees and (2) firms with ≥ 500 employees

6. Should Liability and Workers Compensation Coverage Be Included?

Policy objective: Make available types of insurance that businesses need to sustain economic activity and provide mechanism for compensating injured parties

Proposals	Liability or WC Covered?
BCPP primary	No
PRIA	No
Chubb	No

6. Should Liability and Workers Compensation Coverage Be Included?

Policy objective: Make available types of insurance that businesses need to sustain economic activity and provide mechanism for compensating injured parties

Considerations

- Including these lines adds to program cost
- But program designers should not focus on one aspect of problem to exclusion of other important aspects
- Further work needed to understand implications of liability and workers comp exposure on firm business and risk mitigation behavior

Proposals	Liability or WC Covered?
BCPP primary	No
PRIA	No
Chubb	No

Concluding Thoughts

- The answers to each of these questions can help guide the design of a risk transfer mechanism
- A number of proposals are being floated, and desirable features from each may be combined
- The debate over pandemic risk insurance provides an opportunity to better understand if and how insurance mechanism can remain an integral part of U.S. strategy to address many considerable risks we face



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