Feasibility Questions About Government-Sponsored Insurance for Business Interruption Losses from Pandemics

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IMPORTANCE The COVID-19 pandemic's effects on the closures of businesses has rekindled an interest in pandemic insurance. However, insurers are reluctant to expand their business interruption (BI) products to cover pandemics and attention is now focused on a long-term federal government solution. Legislative attention is currently directed toward the Pandemic Risk Insurance Act (PRIA), which was introduced in May 2020, among other proposals. PRIA, structured similarly to the Terrorism Risk Insurance Act (TRIA), would provide federally-backed BI insurance for pandemics.

OBJECTIVES The authors assert that PRIA in its current form is problematic and discuss two alternative solutions that borrow from the current National Flood Insurance Program (NFIP) and the federal crop insurance program. There is also discussion about the insurance industry-proposed Business Continuity Protection Program (BCPP).

ANALYSIS OF PRIA One critique the authors make about the PRIA bill addresses contract concerns, such as ambiguous wording and potential duplicative compensation between insurers and the federal government. The draft bill also makes two false underlying assumptions about BI insurance, such as associating pandemic-caused losses with the same perils covered by typical BI insurance and assuming BI insurance covers payroll expenses. An additional criticism focuses on PRIA's conflict with fundamental insurance concepts, such as moral hazard, rate-setting and funding, and voluntary participation by insurers. Importantly, an analysis conducted by the authors indicates that even the low insurer retentions under PRIA could expose them to high levels of financial risk in the event of a severe pandemic.

ALTERNATIVE PROPOSALS The authors propose two new alternative frameworks to PRIA and the BCPP: the National Pandemic Risk Insurance Program (NPRIP) and the National Pandemic Risk Reinsurance Program (NPRRP). The BCPP and NPRIP programs would not require private insurers to take on risk, but would allow both programs to set the rates and terms of coverage. The NPRIP, unlike the BCPP, would reimburse a business for at least a portion of lost profits due to a pandemic for more than 3 months. The authors also predict the NPRIP would attract more businesses, but its premiums would be higher because of its broader coverage.

The NPRRP is modeled after the federal crop insurance program and shares some similarities to the NFIP, such as the government setting the rates and terms. However, in the NPRRP model, the government would act as a reinsurer for private carriers participating in the program. The authors further state that loss retentions could be problematic for BI pandemic insurance but suggest insurers could negotiate their retentions with the government commensurate with their financial capacity.

CONCLUSION & RELEVANCE Many challenges exist in creating a viable and efficient federal program for BI pandemic risk. However, the authors argue there are advantages to establishing such programs, such as reducing the uncertainty that many firms face with respect to pandemic-related losses, providing for greater economic stability, and creating a mechanism for pre-event financing. PRIA in its current iteration would be difficult to administer, would be subject to political interference, raises equity issues, and could obligate the government to make payments to businesses that would not be adequately funded by its premium revenues. Regardless of which BI pandemic program is implemented, it is important that it be structured to address the many challenges it would face and achieve the highest possible efficiency and equity.