Financing Losses from Catastrophic Risks

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The views expressed in this paper, are those of the authors and should not be interpreted as those of the Congressional Budget Office.

Introduction

- Growing public role in insuring cat risk
- Industry's stated motivations for subsidized reinsurance are suspect
  - Size (correlation) of losses
  - Difficulty in making estimates of insured losses
  - Role of government in creating losses
- Relevant Questions
  - What factors currently impede private market insurers from amassing more capital for insurance against cat losses?
  - What are the barriers that prevent broader securities markets from directly participating?
  - What types of policy changes could be potentially implemented to reduce these impediments and barriers?

Existing Distorting Policies

- State Rate Suppression and Other Restrictions
- Accounting and Legal Regulation
- Federal Tax Treatment
- Legal Environment
- Crowding Out: State and Federal Levels

Four Reform Options

- Optional Federal Charter for Insurers
- Regulatory Improvement of Risk Transfer Mechanisms with Basis Risk
- Tax Reform
- Auctioning Federal Reinsurance for Cat Risk

Can Private Markets Really Insure the "Big One"

- Corporate vs. personal insurance
- Capital flows into private markets
- Growth of alternative risk management