

October 16, 2017

TO: NAR Insurance Committee
FROM: Donna Smith, Chair, Disaster Policy Work Group
SUBJECT: Disaster Insurance Research Proposal

Recommendation:

- That NAR fund actuarial cost research to guide the development of NAR policy on a national disaster insurance program.

Rationale: Each year, the Federal government spends billions of dollars on disaster relief to repair uninsured homes damaged by natural disasters. The Work Group believes that it would be less expensive to pool the risk, charge a fee on all homeowners insurance policies, and build up a national insurance fund to pay for the losses. However, no actuarial research has been conducted to determine the size of the insurance fund or policy fee needed to cover the nationwide annual cost. This research would be the first to use sophisticated catastrophe modeling in order to evaluate the costs and benefits of a federal insurance fund for three perils (earthquakes, floods, tornadoes) across 48 states.

Findings & Conclusions:

- Private natural catastrophe coverage can be very expensive for high-risk properties.
- Due to the unpredictable nature of the risk, insurers must set rates that exceed losses in most years in order to build up the reserves to cover the potential of anticipated catastrophic years.
- Without some level of government involvement, it may not be possible for private catastrophic loss insurers to provide coverage at a premium level most property owners would pay.
- While not reducing the cost to insure high-risk properties, an all-perils approach could keep rates below full-risk levels for some by expanding the policyholder base over which to spread the cost.
- Given the low voluntary purchase rates of flood insurance (1% in low-risk areas) and earthquake insurance (10% across CA), a mandatory purchase requirement would need to be considered.
- At its core, insurance is about spreading risk among insureds. If there is a way to charge some policyholders less without charging others too much, such an approach is worth exploring.
- On the other hand, how much a federal insurance program would have to charge each homeowner in order to cover the cost is an empirical question requiring new research.

Work Group Members:

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