New York Times Editorial for Insurance Reform

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Editorial

Insurance for the Next Big One

There is impeccable logic to the argument that taxpayers should not be made to pay for the risks incurred by people who choose to live along a hurricane-prone coast or atop a major geological fault.

More than half of all Americans, however, live within 50 miles of a coast. With premiums rising relentlessly and insurers cutting hundreds of thousands of homeowner policies from the Gulf of Mexico up the East Coast to Florida and Long Island, there is a real danger that millions might soon be unable to purchase insurance. That's a compelling argument for government help.

A well-designed program - one that priced insurance in a way that encouraged homeowners to think twice about where they build and local governments to think twice about their zoning policies - could mitigate the so-called "moral hazard" of encouraging people to make riskier choices than they otherwise would. The alternative of millions of Americans' going without insurance is a far worse option.

Since Hurricane Katrina - which caused a record $50 billion in insured losses - private insurers have jacked up premiums as much as they can and, when barred from raising prices, dropped coverage of riskier homes.

Many of these companies, which have turned denying valid claims into an art form, deserve little sympathy and certainly no government subsidies. Still, taxpayers would end up picking up the tab through federal disaster relief if millions of homeowners lost their insurance or decided to drop it due to high premiums.

One idea making its way through Congress is to have the government become the sole provider of hurricane insurance in coastal areas - expanding the National Flood Insurance Program to include wind damage, too. There are also calls to study letting insurers amass reserves in tax-deferred accounts, to prepare for future catastrophes.

Another possible approach would be for the government to offer a backstop to private insurers. The State of Florida has set up a $33 billion catastrophe fund - financed through premiums paid by insurers - to provide reinsurance that kicks in when claims exceed $4.5 billion.

Representatives Ron Klein and Tim Mahoney, both Florida Democrats, submitted a proposal to the House last month that would build on this by setting up a federal catastrophe fund where state funds could pool their risks. A well-designed federal fund would kick in only after claims hit a fairly high cap and would have to properly tie premiums to risks. If done correctly, this would protect private insurers from going bankrupt in the case of a Big One - and enable insurers to provide affordable coverage for homeowners.

Moral hazard, of course, cannot be totally eliminated. There is also the risk that a government fund would be under political pressure to keep premiums low, meaning that it would always be underfunded. But there are times when the need for government protection overrides these concerns. Such is the case with the Federal Deposit Insurance Corporation, which insures Americans' bank deposits to reduce the risk of a bank run that could undermine the banking system.

The tens of millions of Americans who already live in high-risk areas must have access to insurance, and it is time for Congress and the White House to start thinking about how to make sure that happens.