

'Proposed Federal Pandemic Risk Reinsurance Program: What We Know So Far'

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Development of legislation to establish a Federal Pandemic Risk Reinsurance Program appears to be progressing. It has been reported that a bill could be introduced in the US House of Representatives as early as this month. The bill is a priority of House Financial Services Committee Chair Maxine Waters (D-CA).

The Pandemic Risk Insurance Act of 2020 — currently in discussion draft form — would establish the Federal Pandemic Risk Reinsurance Program to provide a “transparent system of shared public and private compensation for business interruption losses resulting from a pandemic or outbreak of communicative disease.” Subject to certain conditions, deductibles and caps, the program would cover insured losses arising from public health emergencies.

The current iteration of the bill envisions a structure that is similar to the Terrorism Risk Insurance Program (TRIP) that Congress passed into law shortly after the September 11, 2001, terrorist attacks. The initial Terrorism Risk Insurance Act (TRIA) was passed in 2002 in order to stabilize the market and ensure that commercial entities—particularly owners of commercial real estate in large cities and owners/operators of “target risks” throughout the country—could purchase terrorism risk insurance. Congress has since reauthorized TRIP multiple times, including on December 20, 2019, when it was extended through 2027.

Like TRIP, the proposed Federal Pandemic Risk Reinsurance Program would be housed in and administered by the US Department of the Treasury. The discussion draft of the bill indicates that the program would apply to certain losses that are covered by business interruption insurance in the event of a pandemic or outbreak of communicative disease. This potential federal initiative comes after several states have announced that they are considering legislation that would compel insurers to retroactively cover certain COVID-19-related losses under business interruption policies that are currently in force.

Key aspects of the program (which are subject to change) include the following.

Eligibility

Insurer participation in the program would be voluntary.

- Eligible insurers would be insurers that receive direct earned premiums for any type of commercial property and casualty insurance coverage, and are:
- Licensed or admitted to engage in the business of providing primary or excess insurance in any state, including non-US insurers listed by the National Association of Insurance Commissioners (NAIC) International Insurers Department
- Approved for the purpose of offering property and casualty insurance by a federal agency in connection with maritime, energy or aviation activity
- State residual market insurance entities or workers' compensation funds
- Certain captive insurers and other self-insurance arrangements, provided that the secretary of the Treasury has determined to include such entities in the program.

Coverage Terms

- Aggregate event deductible (or “trigger”) of \$250 million
- Aggregate annual cap of \$500 billion
- 95% federal share of compensation for insured losses in excess of the aggregate deductible or trigger amount up to the aggregate annual cap.

Key Definitions

- “Insured losses” are losses resulting from a “covered health emergency” that are covered by primary or excess “business interruption insurance” issued by a participating insurer, provided that the loss occurs (i) within the United States, (ii) within an area to which a covered health emergency applies, and (iii) during the period that the covered public health emergency for such area is in effect.
- A “covered public health emergency” is any outbreak of infectious disease or pandemic: (i) for which an emergency is declared under the public Health Service Act, [or] (ii) for which an emergency or major disaster is declared by the president under the Robert T. Stafford Disaster Relief and Emergency Assistance Act, [and/or] (iii) that is certified by the secretary as a public health emergency. (It is currently unclear which prongs must be satisfied.)
- Business interruption insurance is defined as commercial lines of “property and casualty insurance” coverage provided or made available for losses resulting from periods of suspended business operations, whether provided under broader coverage for property losses or separately.
- “Property and casualty insurance” is defined as commercial lines of property and casualty insurance, including excess insurance, workers’ compensation insurance, and directors and officers liability insurance. It does not include:
 - Federal crop insurance issued or reinsured under the Federal Crop Insurance Act, or any other type of crop/livestock insurance, including farm owners multi-peril insurance
 - Private mortgage insurance or title insurance
 - Financial guaranty insurance issued by monoline financial guaranty insurers
 - Medical malpractice insurance
 - Health or life insurance (including group life)
 - Flood insurance provided under the National Flood Insurance Act
 - Reinsurance or retrocessional reinsurance
 - Commercial auto insurance
 - Burglary and theft insurance
 - Surety insurance
 - Professional liability insurance.

Voluntary Participation

Unlike TRIA (where insurers providing certain insurance products must make terrorism risk insurance available), the bill (as currently drafted) would permit insurers to participate in the program on a voluntary basis. Insurers that elect to participate in the program would be charged a premium for reinsurance coverage, to be deposited into a Pandemic Risk Reinsurance Fund maintained by Treasury to pay insured losses and to cover the costs associated with administering the program.

Each insurer that chooses to participate in the program would have to make coverage available in all of its business interruption policies. Participating insurers would not be permitted to offer program coverage on terms, amounts or other coverage-related limitations that materially differ from those that are applicable to losses not related to public health emergencies.

Federal Share of Compensation, Program Trigger, Aggregate Cap on Annual Liability

No compensation would be paid unless the aggregate industry losses resulting from a certified public health emergency exceed a trigger. The trigger is currently set at \$250 million in the discussion draft. As with TRIP claims, the program would only cover losses on policies that

include certain “clear and conspicuous” disclosure language (including disclosure pertaining to the program’s annual cap).

The bill sets an annual cap (currently \$500 billion in the discussion draft) such that neither the secretary of Treasury nor the participating insurers would be liable for paying losses in excess of that amount. Losses above the deductible and below the cap would be covered jointly by Treasury and the participating insurers subject to each insurer’s retention. The federal share of compensation for insured losses under the bill is equal to 95% of the portion of the amount such insured losses exceed the insurer’s deductible, where “insurer deductible” is defined as the value of the insurer’s direct earned premiums during the immediately preceding calendar year, multiplied by a certain percentage (currently set at 5% in the discussion draft).

The bill envisions that the program would pay incurred losses on a pro rata basis, the methodology for which will be determined by the secretary within 240 days of the bill passing into law. Reinsurance purchased by a participating insurer through the private market would not affect the calculation of the insurer’s deductible or retention.

Studies and Reports

Treasury

Like TRIA for terrorism risk insurance, the bill would require participating insurers to submit to Treasury information pertaining to losses arising under business interruption insurance coverage resulting from public health emergencies. The bill as currently drafted would require participating insurers to submit annually the following data to Treasury:

- Premiums earned on such coverage
- Geographical location of exposures
- Take-up rate for such coverage
- Amount of private reinsurance purchased for losses resulting from public health emergencies
- Other matters deemed appropriate by the secretary.

The collected data would serve as the basis for annual studies and reports on the program that, pursuant to the bill, the secretary must submit to the House Financial Services Committee and the Senate Committee on Banking, Housing and Urban Affairs each year.

The bill would also require the secretary to conduct a study that assesses and identifies any competitive challenges small insurers face in the business interruption insurance marketplace, and to report its findings to Congress every other year. Finally, the secretary (in coordination with the NAIC and other stakeholders) would be required to conduct a one-time study on the availability and affordability of insurance for risk of public health emergencies after the program terminates (the current draft of the bill does not provide for a termination date, however).

Other Federal Authorities

The bill also contemplates studies and reports to be undertaken and submitted by other federal authorities. It would require the President’s Working Group on Financial Markets to study and report to Congress on the long-term availability and affordability of insurance for public health emergencies. It also would require the comptroller general to study and report to Congress on any specific markets that have unique capacity constraints on the amount of available business interruption insurance, provide an assessment of factors contributing to any such constraints, and submit recommendations to address those constraints.

Federal Cause of Action

The bill does not explicitly address either proposed state legislation to require insurers to cover business interruption losses for small and/or medium-sized business affected by “public health emergencies” or the proliferating number of suits in which insureds allege that their business interruption coverage should be read to include losses arising from or related to such emergencies. But there is a provision in the bill for a “federal cause of action” for property damage, personal injury or death arising out of or resulting from a covered public health emergency. The federal cause of action, which presumably would at a minimum encompass business interruption losses covered by policies issued by participating insurers, would be the exclusive remedy for such claims and a powerful incentive for insurers to participate in the program. This section of the bill would preempt all state causes of action and, among other things, would provide the federal government with the right of subrogation with respect to any payment or claim paid by the United States under the bill.

As with all sections of the discussion draft, the “Litigation Management” section of the bill is a work in progress and presumably will be the subject of further discussion. McDermott Will & Emery is monitoring this space, and will update this analysis accordingly.

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