

7. (2.75 points)

a. (0.75 point)

For each of the following types of insurance, briefly describe the extent to which private insurers provide coverage.

- Crop insurance
- Unemployment insurance
- Terrorism insurance

b. (1 point)

For each of the following government insurance programs, briefly describe a unique social cost, and propose a change to each program that could mitigate the cost.

- Federal Crop Insurance Program
- Federal-State Unemployment Insurance Program

c. (1 point)

Describe one argument that supports and one argument that refutes the following statement: The Terrorism Risk Insurance Program is necessary.

SAMPLE ANSWERS AND EXAMINER'S REPORT

QUESTION 7	
TOTAL POINT VALUE: 2.75	LEARNING OBJECTIVE: B2, B3
SAMPLE ANSWERS (BY PART, AS APPLICABLE)	
Part a: 0.75 point	
The following provides two examples of thorough responses having the necessary components to demonstrate knowledge of the topic and obtain full credit:	
<p>Sample answer 1</p> <ul style="list-style-type: none"> • Crop -> Private insurers write and service policies, and the federal government reinsures • Unemployment -> Do not provide coverage • Terrorism -> Private insurers write and service policies, and federal government reinsures <p>Sample answer 2</p> <ul style="list-style-type: none"> • Crop Insurance: Private insurer in partnership with government. Private insurer market and service the policy. Private and government share the profit & loss • Unemployment: No involvement of private • Terrorism: Private partnership with government. Private market and service the policy. Government as a reinsurer. It pays for the loss if exceeds a certain amount. (20% deductible. After 20% deductible, pay 85% of the loss) 	
Part b: 1 point	
The following provides two examples of thorough responses having the necessary components to demonstrate knowledge of the topic and obtain full credit:	
<p>Sample answer 1</p> <ul style="list-style-type: none"> • Crop – Insurance encourages overproduction – could only provide insurance up to a certain amount of land/product • Unemployment – studies show it lengthens time of unemployment -> reducing benefits would increase incentive to get a new job more quickly <p>Sample answer 2</p> <ul style="list-style-type: none"> • Crop Insurance: The sharing of loss between government and private has not been equal. Historically, private has gain, but government experienced loss. The loss of government will eventually be burden in taxpayer. The proposed change in balance the sharing between private sector and government • Unemployment Insurance: Unemployment insurance has shown to elongate unemployment period. This is a social cost for general population. A proposed change is to encourage job-hunting during unemployment 	
Part c: 1 point	
The following provides examples of thorough responses having the necessary components to demonstrate knowledge of the topic and obtain full credit:	
<p>Sample answer 1</p> <ul style="list-style-type: none"> • Support – the insurance industry can't insure a catastrophic, non-fortuitous event like terrorism. And the collateral social benefit of avoiding economic disruption in the event of a terrorist event is too large to cover. • Against – Participation is fairly low and the private industry may be able to cover through risk exchanges and cat bonds. <p>Sample answer 2</p>	

SAMPLE ANSWERS AND EXAMINER'S REPORT

- Supports: It serves a social purpose to prevent economic disruptions following a terrorist attack and private insurance sector is unwilling to offer terrorism insurance.
- Refutes: We haven't had a terrorist attack since 9/11, and pre-9/11, private insurers were able to provide coverage. They should be recovered enough by now to do the same. TRIA was meant to be temporary and eventually handed back to the private insurance sector.

Sample answer 3

- For: The private market will not support terrorism coverage due to the fact that losses are not fortuitous, that it does not affect enough people to produce stable rates, and that losses can be catastrophic. Gov't fills the void in coverage, and provides a social good.
- Against: the industry is well capitalized enough so that the TRIP program is unnecessary and an additional cost that is not needed; it also may encourage insurers to be lax in their U/W standards & aggregation monitoring if they know backstop is there.

Sample answer 4

- Necessary: Terrorism is an uninsurable event—it is not random or accidental and there is not enough experience to accurately price. Therefore, it is not available or affordable in the private market.
- Not necessary: Hasn't had a major terrorist event in the past 10 years, partly due to more stringent conduct of other industries (aviation, defense). Should be okay to remove program.

EXAMINER'S REPORT (BY PART, AS APPLICABLE)

Part a

Candidates generally performed well on this part. Candidates were expected to know the relationship between private insurers and government, e.g., whether a partnership exists between private insurer and government and how it works at a high level.

When there's a partnership between private insurers and government, e.g.: crop insurance and terrorism insurance, full credit would be awarded for stating the partnership with the program name; or describing how the private insurers and government function in the relationship. Simply stating no involvement in unemployment insurance would receive full credit for this subpart.

A common error observed for crop insurance was stating that it is exclusively provided by the government, and a common error for terrorism coverage was stating that it is not provided by the private insurers. Most candidates stated the correct answer for unemployment; there were no common errors.

Part b

Candidates were expected to identify a unique social cost for crop insurance and unemployment insurance program, and a reasonable mitigation solution.

This question was challenging for many candidates. The question specifically asked for a unique social cost. However some candidates provided a generic social cost that is common to many government programs, such as subsidy from the government. Further, many provided a flaw of the program instead of a social cost brought by the program, such as awareness of the program is low. Also, a good amount of candidates described the funding mechanism of the program. None of these answers were awarded credit.

SAMPLE ANSWERS AND EXAMINER'S REPORT

For those candidates that were able to identify a unique social cost, they were also able to propose a change to each program that could mitigate the social cost.

Despite not asked in the question, many candidates answered how the programs work and how it benefits the insureds. No credit was given for this response.

Part c

Candidates were expected to construct an argument for both sides, and elaborate on the argument.

Majority of candidates received at least partial credit on part c, but fewer were able to draft out the argument and elaborate to receive full credit. Most of the responses from candidates were considered correct or reasonable, though a simple correct statement without supporting facts or elaboration would not earn full credit for this part.