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The Geneva Association - General Secretariat - 53, route de Malagnou - CH-1208 Geneva
Tel.: +41-22-707 66 00 - Fax: +41-22-736 75 36 - secretariat@genevaassociation.org - www.genevaassociation.org

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Layout & Distribution: Valéria Kozakova & Bernadette Curty

Alternative Instruments for Financing Long-Tail (Liability) Risks

Jan Pieter Six

Liability risks: present & future

- *accidental* liability risks
 - no major problems, calculability OK
 - no crisis to be expected
- *long-tail* liability risks
 - major problems, calculability not OK
 - crisis to be expected, caused by:
 - # emerging/new risks + legal developments
 - # *open-ended* nature of liability insurance

Conclusion

**(Dynamic) liability law and
(open-ended) liability insurance
are *no longer*
adequate instruments
for financing
long-tail (liability) risks**

Traditional “solutions”

- premium increase
- (higher) deductibles
- lower limits
- stricter conditions
- exclusion of specific risks
- better risk differentiation

>> open-ended nature *unchanged*

>> no *structural* solutions

Alternative solutions

- funds?
- first-party insurance
- “*direct*” insurance
- insurance pools

Funds

- wide variety of funds
- advantages over-estimated
- same problems as with liability
- accumulation risk:
 - funds - limited (to size of fund)
 - insurance - unlimited

First-party insurance

- victim = *first* party, with own policy (e.g. Fire)
- victim has *contractual* right to be compensated
- private or group insurance
- premium paid by victim or other party (e.g. employer)

“Direct” insurance -1-

- victim = “*third*” party, covered on policy of someone else (e.g. neighbour), who pays premium
- third party has ***contractual*** right to be compensated
- ***no*** open-ended nature
- liability law deliberately circumvented

“Direct” insurance -2-

- liability law deliberately circumvented >>
 - **strict(er) definitions** possible (e.g. on causality)
 - **fixed** compensation possible (e.g. for pain & suffering)
- >>better risk *differentiation* by insurer
>>better risk *management* for insurer

Examples of direct insurance

- CAR – damaged goods of third parties
 - Environmental Damage Insurance (NL) (took 8 years to develop understand and!)
 - Medical Experiments on Humans (NL)
 - Garantie contre les Accidents de la Vie (F)
 - Occupational Diseases??? (NL)
-
- NB: see (positive) literature (Bocken/CEA1997, Faure et al.)

Insurance pools

- wide variety of pool-constructions
- prerequisite: coöperation between insurers
- competition-proof?
- only for experimental phase?
- ***additional*** mechanism to manage and spread risks
- NL: Env. Damage Insurance pooled

Final conclusions

- open-ended nature is key problem
- several alternatives
- “direct” insurance most creative alternative
- proven track record: it works & works well
- many supporters in scientific world
- increasing political support

>>>>> ***try it !***