ABSTRACT:

This talk highlights factors that lead individuals not to protect themselves against low-probability high-consequence events until it is too late, and the role that the private and public sectors can play to deal with this problem. I will focus on the flood and hurricane risk that individuals face in hazard-prone areas since the U.S. Congress is studying the reauthorization of the National Flood Insurance Program that expires on November 30, 2018. The errors that individuals exhibit in deciding not to purchase insurance or invest in loss reduction measures prior to a disaster can be traced to the effects of six decision biases: myopia, amnesia, optimism, inertia, simplification and herding. Along with two guiding principles for insurance, a behavioral risk audit using concepts from choice architecture coupled with economic incentives can assist in designing strategies to encourage property owners in hazard-prone areas to purchase insurance and invest in cost-effective adaptation measures to protect themselves against future disaster losses.