RIMS
the risk management society

September 16, 2013

Federal Insurance Office
Attn: Kevin Meehan, Room 1319 MT
United States Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington D.C. 20220

Re: President's Working Group on Financial Markets: Terrorism Risk Insurance Analysis

Dear Mr. Meehan:

On behalf of the Risk and Insurance Management Society, Inc. (RIMS), these comments are submitted in response to a request published in the July 16, 2013 Federal Register. This request was published pursuant to Terrorism Risk Insurance Program Reauthorization Act of 2007 requiring the President's Working Group on Financial Markets to conduct an ongoing analysis, and submit a report to Congress on, the availability and affordability of insurance for terrorism risk. The solicitation for comments includes a series of topics which respondents are invited to address. Our comments will be largely confined to those topics that most directly pertain to our membership, interests, and policy positions.

RIMS is a not-for-profit organization dedicated to advancing the theory and practice of risk management for the benefit of our membership. Our discipline is vital to the creation and protection of physical, financial, and human resources. RIMS is the largest organization of risk management professionals, representing over 11,000 members worldwide from more than 3,500 entities. Membership includes both public and private entities and spans the entire economic spectrum from the high-tech sector, real estate, financial, healthcare, energy, transportation, education, and defense.

Summary of RIMS Position

One of the basic functions of risk management is the identification of potential risks to an organization and the subsequent identification of methods for mitigating those risks. Insurance coverage is a necessary component in managing risk, especially those risks that can result in catastrophic losses. Terrorism is one such risk that presents catastrophic exposures to our member organizations. It is vital that terrorism insurance continue to be available to commercial insurance consumers at affordable rates beyond the current December 31, 2014 expiration date set for the TRIA program.

RIMS has consistently advocated for the necessity of TRIA and continues to advocate for a long term extension beyond the current expiration date of December 31, 2014. We feel very strongly that the availability and affordability of adequate insurance coverage for acts of terrorism is not only an insurance problem, but also an economic one. The aftermath of 9/11 proved that the private insurance market alone is likely not able to provide adequate coverage at prices that our members can afford. This will force many organizations to self-insure thus placing their entire business future at risk in the event of a terrorist attack. Additionally, with limits of terrorism insurance required by lenders unavailable at commercially reasonable costs, businesses may be unable to secure financing for current and future projects, thus stunting a fragile improvement in our economy.

RIMS supports the following principles in the development of a long term solution to the TRIA program:

- A public/private partnership provides the best alternative to addressing the long-term needs of availability and affordability of terrorism insurance. A completely private market solution likely is still not feasible due to the difficulty in predicting and modeling for acts of terrorism.

- A program should always be in place that will ensure an orderly and efficient response to acts of terror in order to minimize market disruptions and ensure that benefits are available to all victims. An orderly program to address terrorism losses will avoid wasteful government spending which often accompanies an unplanned, haphazard response to such an event.

- Any solution needs to address the long-term availability and affordability of insurance coverage for nuclear, biological, chemical and radiological terrorist events (NBCR).

Negative Impact of TRIA Termination

A. Availability and Affordability of Terrorism Coverage

Prior to the September 11, 2001 attacks it was common for terrorism coverage to be included in general insurance policies with no specific cost to the consumer for terrorism coverage. The risk, at the time, was considered to be negligible. Following 9/11, insurers reassessed the risk of terrorism and began to offer terrorism coverage only in specialized policies with very restricted limits. The coverage was available only at prices that many consumers were simply unable to afford.

The lack of adequate capacity at affordable rates led to significant concerns to many industry sectors and the U.S. economy as a whole. In February of 2002 the Government Accountability Office stated that the "resulting economic drag" from difficulties in obtaining adequate terrorism coverage could "slow economic recovery and growth." During September of 2002, Moody's Investors Services downgraded the rating on $4.5 billion in loans on commercial properties due to lack of terrorism coverage while a survey by the Real Estate Roundtable found that "$15.5 billion of real estate projects in 17 states were stalled or canceled because of a continuing scarcity of terrorism insurance."

Passage of TRIA in 2002 brought stability to this highly volatile situation. By allowing private insurers to shift some of the terrorism risks to the federal government, the private market was able to free up capacity which could then be made available to consumers. A 2013 survey of RIMS membership shows that capacity is also generally not an issue at this point in time. Ninety-two percent of respondents to this survey answered that they have been able to obtain adequate terrorism coverage over the past 18 months. This is up from the 84% who had no trouble obtaining coverage in a similar survey conducted in 2010. The availability of adequate terrorism coverage is directly linked to the existence of TRIA.

However, while there may be some increased private insurer capacity, if TRIA is allowed to expire, there will once again be uncertainty within the marketplace that impacts affordability and availability of terrorism coverage. If the private market is forced to assume all terrorism risks, then carriers will look to reduce their exposure, particularly in certain high-threat areas like the Northeast. As a result, pricing for this more limited amount of coverage would rise.

The 2013 RIMS survey found that 69% of respondents expect those limits would decrease or that coverage would not be offered at all if TRIA were not in existence. Without adequate coverage, many of these organizations will be forced to self-insure. In the event of major terrorist attack, most businesses would be unable to absorb the losses forcing the business to fail. Businesses that can absorb the costs of a terrorist attack would do so at the expense of other business growth initiatives, namely investment in further growth of their business. This will have a negative impact on the economy at a time when the economy would be looking to recover from the after-effects of a terrorist event.

B. Impact on Captives

Many larger insureds assume losses from terrorist events through the use of captive insurance companies. These companies are eligible for TRIA participation which provides them with the security of the federal government backstop. If TRIA is allowed to expire, many of these captive insurers will become susceptible to failure in the event of a catastrophic loss. If the captive insurer fails due to terrorism losses, it will likely also fail to protect against other lines of coverage unrelated to the terrorist event, but which are insured through the captive's programs. Few businesses will be able to absorb the resulting uninsured losses.

C. Impact on Lending

Since the 9/11 attacks, most commercial lenders have required terrorism insurance be purchased to secure commercial construction and mortgage loans. Immediately following 9/11 it was difficult for commercial policyholders to secure coverage for terrorism risk, yet it was required to secure or maintain financing. According to the Coalition to Insurance Against Terrorism (CIAT) testimony before Congress on September 11, 2012 over $15 billion in real estate transactions were "stalled or even cancelled" due to a lack of terrorism coverage in the 14 months following 9/11. Further, CIAT cited a White House Council of Economic Advisors statistic confirming the loss of 300,000 jobs from deferred construction investment.

In 2005, as TRIA approached expiration, many insurers placed sunset provisions into their policies to address a lack of coverage should TRIA have been allowed to expire. This led to significant uncertainty in the financial and construction financing markets. Lenders had no intentions of removing loan requirements for terrorism coverage, yet coverage was set to expire upon TRIA expiration. As commercial insurance policies will be coming up for renewal in early 2014, we expect these same sunset provisions to be inserted into policies resulting in the same uncertainties faced in 2005 without a timely reauthorization of TRIA.

D. Impact on Workers Compensation and Other Coverages

As mentioned above, if the private market is forced to assume all terrorism risk, they will look to reduce their exposures. This will certainly be true for property coverage, but also for workers compensation coverage. In some modeling it is estimated that workers compensation losses will constitute 25% of all commercial property and liability losses from a terrorist attack.

The RIMS membership survey found that many insurers are already careful to avoid concentration of exposures. Sixty-three percent of respondents reported requirements from their workers compensation insurers for submittal of information on their organization's concentration of employees within a single location. While only roughly 6% have been declined coverage to this point because of a high concentration of employees, 20% anticipate having trouble obtaining coverage if TRIA is not reauthorized.

Without TRIA a catastrophic terrorism event could also potentially affect many other lines of coverage. While insurance reserves are segregated by lines, an insurer's losses ultimately end up on the same balance sheet. If a carrier suffers significant losses due to a terrorism event it could lead to a limiting of coverage or higher prices for other coverage lines as the insurer looks to mitigate its overall losses.

Insurance Market Considerations

A. Difficulty in Modeling for Terrorism

In spite of some recent statements that acts of terrorism can be modeled like natural catastrophes, terrorism risk lacks certain elements possessed by catastrophe risks such as hurricane or earthquake. The resulting losses from most risks are accidental and the risks themselves are generally predictable. Terrorism risk lacks both elements. The losses from terrorist events are far from accidental as they are the direct result of deliberate human behavior and action. A plot must be hatched and then executed by one or more individuals. The motives, targets and actions of the perpetrators are constantly changing and may be affected by government actions which modelers and insurers are not aware of.

Terrorism is also inherently unpredictable. Insurers can accurately predict which parts of the country will be hit by hurricanes or tornadoes, what time of year these events are most likely to occur, and what the anticipated losses will be based on the severity of the event. They are able to do this based on historical experience and data. Thankfully, this data does not exist for terrorism risk because of the rarity of such events occurring.

Weather prediction accuracy is also enhanced by studying near misses and variances in weather that resulted in a storm missing a target or having its impact lessened. With terrorism risk, this information is often highly classified and not available to modelers. This lack of data adds to the difficulties faced in predicting terrorism events.

Predicting severity of losses from a terrorist event is also difficult due to the wide range in severity of potential attacks. For example, losses from the 9/11 attacks have been estimated in the $35 billion range while preliminary estimates of business losses from the Boston bombings have been closer to $10 million. Attempts to model terrorism events rely on specific assumptions about the method of attack, weapons used, and specific sites that will be attacked. While this information can be useful in strengthening a specific property's risk of loss, it is not as useful in attempting to assess potential risk exposures for a wider geographic area. Thus, efforts to model and underwrite for acts of terrorism are far too rudimentary to be reliable enough for insureds to cover such potential losses without TRIA.

Suggested Revisions/Modifications

A. Certification Mechanism

The Boston Marathon bombing has raised questions about how the certification process is currently handled under TRIA. To date no formal declaration has been made as to whether the event will or will not be certified as an act of terrorism under TRIA. This has led to a great deal of uncertainty as insurers and policyholders are unsure as to which claims will or will not be paid and/or covered under TRIA. If the event is certified then those policyholders who chose to not have coverage may be unable to recoup their losses. If the event is not certified then those who did elect to obtain terrorism coverage may not have their claims paid. This process should be made clearer so that such confusion does not result from future attacks.

Under the current program a terrorist act must be certified by the Secretary of the Treasury in concurrence with the Attorney General and Secretary of State. The process would be more efficient by consolidating this decision making authority within one office or department. A 60 day deadline, with the possibility for one extension, should also be incorporated so that policyholders and carriers will know exactly when a determination will be made, and the claims payment process can begin. The definition for an act of terrorism under TRIA should also be reviewed to ensure that there is a clear definition of what will or will not be considered a terrorist event.

B. NBCR Coverage

The current TRIA program neither explicitly includes nor excludes NBCR events, which has prompted many insurers to exclude NBCR events from terrorism policies based on long-standing standard exclusions for nuclear and pollution risks. As a result consumers are generally unable to obtain NBCR coverage. Based on our survey results, only 23% of respondents currently have coverage for NBCR events. Fifty-eight percent of those who do not have coverage are unable to procure coverage because either it is not offered by their insurer or it is not affordable; yet 83% of respondents believe that NBCR coverage should be made available.

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RIMS supports the inclusion of NBCR coverage in a long term extension of the TRIA program. NBCR events have a high probability of resulting in catastrophic losses for organizations affected by such an attack. Without coverage these organizations are at risk of going under should catastrophic losses occur. In such an event it is likely that the federal government will step in to provide assistance to these organizations, but without a TRIA style public/private loss sharing mechanism in place. By including NBCR in the TRIA program, both sides will know their responsibilities to consumers should such an event occur.

On behalf of RIMS, I want to thank the President's Working Group on Financial Markets for the opportunity to comment on the importance of the TRIA program in ensuring the availability and affordability of terrorism coverage. Should you require additional information, or have any questions, please do not hesitate to contact RIMS Senior Government Affairs Manager, Nathan Bacchus, at 212-655-6215 or nbacchus@rims.org.

Sincerely,

John R. Phelps
RIMS 2013 President

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