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REAUTHORIZING TRIA: THE STATE OF THE TERRORISM RISK INSURANCE MARKET

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

ON

REAUTHORIZING THE TERRORISM RISK INSURANCE ACT (TRIA)

SEPTEMBER 25, 2013

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C O N T E N T S

WEDNESDAY, SEPTEMBER 25, 2013

WITNESSES

Additional Material Supplied for the Record

REAUTHORIZING TRIA: THE STATE OF THE TERRORISM RISK INSURANCE MARKET

WEDNESDAY, SEPTEMBER 25, 2013

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:05 a.m. in room SD–538, Dirksen Senate Office Building, Hon. Tim Johnson, Chairman of the Committee, presiding.

OPENING STATEMENT OF CHAIRMAN TIM JOHNSON

Chairman JOHNSON. Good morning. I call this hearing to order.

Two weeks ago, we observed the 12th anniversary of the tragic September 11 terrorist attacks on our country. In the aftermath of the tragedy and after suffering steep losses, insurance companies stopped offering terrorism insurance coverage as part of their commercial property policies. This had a destabilizing impact on various parts of our economy.

Congress responded by creating the Terrorism Risk Insurance Program to provide a narrow and targeted Government backstop for this insurance coverage. The program proved helpful, creating certainty for many businesses, including developers, construction companies, commercial lenders, as well as private insurance markets.

The program has since been reauthorized by Congress twice. The last time, Congress made very few changes and extended the program for 7 years. It is my hope that, once again, we will be able to find bipartisan consensus for the reauthorization of TRIA well before the program expires at the end of 2014.

While a few may seek dramatic changes or even try to eliminate the program, we should remember that taxpayers have not lost any money on the program. The program's unique structure has fully protected taxpayers while promoting economic growth by preventing interruption in insurance coverage and providing certainty for commercial property developers working on stadiums, universities, malls, and other projects across the country.

Today, we review the state of the terrorism risk insurance market and look forward to hearing from our witnesses about how the current program has functioned and the ongoing need for the same limited Government backstop we already have in TRIA.

With that, I turn to Ranking Member Crapo for his opening statement.

OPENING STATEMENT OF SENATOR MIKE CRAPO

Senator CRAPO. Thank you, Mr. Chairman.

I welcome each of our witnesses today to this important hearing on the Federal Terrorism Risk Insurance Act.

This program's initial passage was in large part due to the inability of businesses to acquire terrorism coverage in the aftermath of the attacks of September 11, 2001. Since then, the program has been reauthorized by Congress two more times, each time with changes that scaled back the exposure to the Federal Government and the taxpayers. With the current program set to expire at the end of 2014, it is appropriate for us to examine how well the program is working, how else we might increase private sector participation in the insurance and in the reinsurance markets.

Terrorism risk, by its nature, is difficult to predict. The size, severity, and frequency of attacks are hard to model. They also may be highly correlated, making it challenging for private insurers to diversify their risk. One of the purposes of passing the original legislation was to give the market time to find innovative solutions to these problems. I am interested in hearing from the witnesses their perspectives on how the private market has evolved in the 12 years since the initial passage of TRIA.

Getting terrorism risk insurance right is important in order to limit economic and physical impacts of any future terrorist attacks on the United States. A properly balanced Terrorism Risk Insurance Program can increase the Nation's resilience to terrorism. However, a program that is too heavily reliant on Federal support can deter the private market from coming up with cost effective solutions.

One of the challenges associated with any Government insurance is getting the pricing right. In TRIA, there is no up-front charge to private insurers for the Government reinsurance and backstop, only post-event cost sharing. Does the current approach make the most sense for taxpayers?

Mr. Beshar's written testimony mentions the business deductible, the aggregate loss threshold, and the business coinsurance as a few of the policy levers we can adjust that may help to better protect taxpayers from shouldering private sector losses. I look forward to the thoughts of the panel as to what impact these changes would have on the willingness of insurers to underwrite terrorism risk.

I am also interested in hearing how well the reinsurance market is developing. Does the current program dampen the reinsurance market's incentives to innovate and find new ways of offering coverage?

As I mentioned previously, each reauthorization has put more private capital in front of the Government backstop. Currently, the Federal Government would recoup any TRIA payments up to $27.5 billion. This industry retention level allows the taxpayer to recover TRIA payments through an industry-wide assessment on property casualty policies and was last changed in the 2005 reauthorization. Should that amount be increased?

And, last, should we look at the approaches that other countries have developed to the challenges presented by terrorism risk? For example, most developed countries charge the insurance industry up front for reinsurance.

As it has been 6 years since we last studied the issue in depth, we now need to examine this program in detail, and Mr. Chairman, I look forward to hearing the witnesses' testimony and their insights into these important policy issues.

Chairman JOHNSON. Thank you, Senator Crapo.

Are there any other Members who would like to give brief opening statements?

Senator HELLER. Mr. Chairman, if I may——

Chairman JOHNSON. Yes.

STATEMENT OF SENATOR DEAN HELLER

Senator HELLER. Thank you very much, and I will be brief. I just want to thank you and the Ranking Member for holding this, what I consider to be a very important hearing. I want to thank those that are here on the panel, also, for taking time with this discussion.

I do not have to tell many here that terrorism is a nationwide threat and it can happen in any city on the East Coast, West Coast, but also in rural America. And, unfortunately, the threat for terrorism is very high in a city like Las Vegas. I like to tell people that there are two Statutes of Liberty in this country and one happens to be in Las Vegas. But, as you know, Nevada's economy is very, very heavily dependent on tourism and a terrorist attack, obviously, would be devastating, not just obviously for the city, but, obviously, the State as a whole.

So, I look forward to working with you, Mr. Chairman, with the Ranking Member, and all my colleagues here on this Committee to see if we can put together some kind of a bipartisan agreement to reauthorize TRIA.

Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you.

I would like to remind my colleagues that the record will be open for the next 7 days for additional statements and any other materials.

Before we begin, I would like to introduce our witnesses that are here with us today.

Mr. Peter Beshar is the Executive Vice President and General Counsel for the Marsh and McLennan Companies, which issued a report on TRIA earlier this year.

Dr. Robert P. Hartwig is the President of the Insurance Information Institute and has written extensively on the issue we are discussing today.

And, finally, Dr. Erwann Michel-Kerjan, who is a Professor and Managing Director of the Risk Management and Decision Processes Center at the Wharton School of Business at the University of Pennsylvania.

Mr. Beshar, you may proceed.

STATEMENT OF PETER J. BESHAR, EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL, MARSH & McLENNAN COMPANIES

Mr. BESHAR. Chairman Johnson and Members of the Committee, I am Peter Beshar and I am grateful for the opportunity to speak with you this morning about TRIA.

Terrorism is a deeply personal issue for Marsh and McLennan. In the attacks on the World Trade Center, our company lost 295 employees and scores of other business associates. Marsh and McLennan also has a unique perspective on the terrorism insurance market. Through our market-leading brands, Marsh and Guy Carpenter, we provide analytics and broking services to all the participants in the terrorism market, the buyers and sellers of terrorism insurance and also key reinsurers.

We consider TRIA to be a model private-public partnership. In the critical moments after 9/11, the TRIA facilitated critical stability into the insurance marketplace, and today, it continues to provide the backstop for a well functioning market. Accordingly, we strongly endorse its reauthorization.

This morning, I would like to briefly cover four areas: First, the current state of the terrorism marketplace; second, the level of capital in the reinsurance industry; third, our recommendations for reforming TRIA; and finally, if TRIA is not renewed, two cautionary notes about the potential impact.

Chairman, as you mentioned, Marsh released a sweeping survey this spring of over 2,500 of our clients in the terrorism insurance marketplace and there were two broad take-aways from that survey. The first is that take-up rates are strong—over 55 percent—across the country. Senator Heller, as you said, in the West, rates are increasing, in the South, in the Midwest. So this is not simply a phenomenon in the Northeast.

The second is that we surveyed industries across the country and the take-up rates are strong—over 70 percent—in the health care industry, amongst media companies, interestingly, amongst nonprofits and educational institutions, as well as real estate developers. So the interest in this coverage across the country and across industry is very strong.

Second, the level of capital in the reinsurance industry has increased in the last 5 years. Our subsidiary Guy Carpenter released a report several months ago indicating that the amount of capital in the reinsurance industry is about $195 billion globally for all risks. That is up from about $160 billion 5 years ago.

Now, to be sure, not all of that capital is available to underwrite this risk of terrorism. Indeed, there are many capital providers who are not interested in underwriting this peril because of how difficult it is to model and for other reasons. Nonetheless, the level of capital in the reinsurance industry has gone up, and if these trends continue, it is our belief that there is capacity for the private sector to continue to expand and thereby reduce the position of the Federal Government and the taxpayer.

So, against this backstop, we would like to offer three recommendations to reform TRIA.

First, we recommend that Congress specifically clarify that if a coverage is provided for all forms of terrorism, including NBCR if there is coverage provided on the underlying policy for that risk.

Second, a lot has happened since Congress last reauthorized TRIA. Cyber risk is clearly a new and more profound risk that we think needs to be grappled with, and Congress should analyze the best way of ensuring that in the event of a catastrophic cyber attack, that TRIA would respond to that.

And, finally, we recommend that we establish—that Congress establish a timeline—we have suggested 90 days—for actually making the certification of whether a terrorist event has occurred and TRIA is, therefore, implicated.

If TRIA is not renewed, just two cautionary notes. First, in the property and casualty market, the "make available" provision, we think, is critical for having induced property and casualty carriers to, in fact, underwrite this risk. And if TRIA were pulled back and that requirement were removed, we think it is highly likely that many property and casualty insurers would stop underwriting this risk.

And, second, very briefly on workers' comp, this is an unusual area of insurance where the carriers are required to provide the coverage without regard to the cause of it, whether it is an accident, an act of war, or an act of terrorism, and we have already begun to see, because of the uncertainty on TRIA, carriers in the workers' comp marketplace have begun to pull back.

So, just in sum, Mr. Chairman, we think this has been a tremendous program and it, in fact, has been a program that has served to protect taxpayers against the risk of a catastrophic loss. Thank you.

Chairman JOHNSON. Thank you.

Dr. Michel-Kerjan, please proceed.

STATEMENT OF ERWANN O. MICHEL-KERJAN, MANAGING DIRECTOR, CENTER FOR RISK MANAGEMENT AND DECISION PROCESSES OPERATIONS AND INFORMATION MANAGEMENT DEPARTMENT, THE WHARTON SCHOOL, UNIVERSITY OF PENNSYLVANIA

Mr. MICHEL-KERJAN. Thank you, Mr. Chairman.

Let me open by saying that if our common goal is to make the Nation more financially resilient to future terrorist attacks and also to limit the spending of taxpayers' money, then our debate should not be on whether to let TRIA expire. Rather, it should be on how we work together to make TRIA more effective.

Indeed, without TRIA, American taxpayers may actually end up paying much more than they would today after a terrorist attack, especially if insurance companies radically lower the capacity they provide under the current monetary requirements when TRIA expires. Indeed, denying Federal disaster relief for uninsured losses after such an attack at a time when our Nation would be under massive stress would be very hard to do for any Congress. There have been so many precedents in recent years with hundreds of billions of dollars spent in Federal relief for natural disaster and corporate bailouts alike.

Still, I do not think a straight reauthorization would be possible, either, for the reasons this Committee stated earlier. So, one should probably continue to reduce Government exposure by increasing the private sector risk sharing, as the previous extension did. But this needs to be done in a way that does not disrupt the market.

As a neutral party, our team at the Wharton School has released over 20 publications on terrorism insurance markets since 2001, more than any other organization. These studies can be used by Congress to make more informed decisions in the coming months.

For instance, we have recently shown that insurance companies have provided much more capacity for terrorism risk than they have for other catastrophic risks because they collect all the premiums but are responsible for only a portion of the losses. This is what TRIA was designed to do.

Terrorism insurance prices in the U.S. have been going down continuously, as Mr. Beshar mentioned. Let me also add here that these are among the least expensive terrorism insurance prices in the world.

In other new analyses that I mentioned in the written testimony, we show that the demand for terrorism insurance for medium and large corporations is not only strong, but also very price inelastic, meaning low sensitivity to price. We found that increasing the premium by 10 percent would only decrease the quantity of terrorism insurance that these firms will buy by one or 2 percent. That means that if TRIA were to be modified and insurers' deductibles were slightly increased from the current 20 percent, most likely, we will not see any impact on the market. Similarly, there was no significant demand change when previous deductible levels had been increased.

Still, about four out of ten large corporations do not have coverage against terrorism today. I think this is something we should be concerned about. Let us remember that on 9/11, the coverage was virtually 100 percent, which allowed for a quick economic recovery of our country.

Also, and this is an important point, we know little about terrorism insurance penetration for small businesses, even though they are the most vulnerable to financial shocks. Congress may want to request a study on small businesses and TRIA.

Before I conclude, let me also say that we must look at how other countries have approached terrorism insurance, because American corporations compete with foreign firms. These firms benefit from these other programs in their own countries. My written testimony looks at Australia, France, Germany, India, Israel, the U.K., and Spain. Note that several of these programs are permanent in nature. Those that are temporary have all been renewed in recent years.

To summarize, TRIA has worked as intended and has sustained a robust terrorism insurance market, especially for large corporations across the country. If TRIA is to be modified to increase the portion of the risk covered by the private sector or for the Government to start charging for its backstop, I think there is room to do so under current market conditions, at least according to our studies. Of course, open issues remain for small businesses, NBCR, cyber risk, and the larger role that the reinsurance industry could play.

In the end, it is how we best use the insurance infrastructure in partnership with the Government to assure effective and equitable solutions are in place that will make our economy terror-proof. This is why, to me, the debate about TRIA is not an insurance issue only. More fundamentally, it is as much a national security and economic competitiveness issue, too.

On behalf of the Wharton School, we look forward to working closely with you in the coming months on how we do that together. Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you.

Dr. Hartwig, you may proceed.

STATEMENT OF ROBERT P. HARTWIG, PH.D., CPCU, PRESIDENT & ECONOMIST, INSURANCE INFORMATION INSTITUTE

Mr. HARTWIG. Thank you, Mr. Chairman. Thank you, Senator Johnson, Ranking Member Crapo, and Members of the Committee. I appreciate the opportunity to have been asked before the Committee to provide testimony on TRIA and the market for terrorism insurance in the United States.

The terrorist attacks of September 11, 2001, produced insured losses larger than any natural or manmade event in history. Claims paid by insurers to their policyholders eventually totaled $42 billion in today's terms. The sheer enormity of that loss, combined with the possibility of future attacks, led insurers to exclude coverage arising from acts of terrorism from virtually all property and liability policies in the commercial sector. Only when TRIA was enacted by TRIA in late 2002 did stability finally return to the market and coverage for terrorist attacks resumed.

Eleven years later, the war on terror is far from over, as the recent Boston Marathon bombings attest. But TRIA is, by all objective measures, an unqualified success. The program not only succeeded in restoring stability to the country's vital insurance and reinsurance markets, but it has done so at little or no cost to taxpayers. The unambiguous success of TRIA demonstrates that the Act has become an indispensable component of the country's national security infrastructure.

In the absence of TRIA, the country is unnecessarily vulnerable and exposed to economic instability and recession. With TRIA's expiration now a little more than a year away, it is virtually certain that terrorism exclusions will soon appear in the market, and it is estimated that 70 to 80 percent of the commercial property market will be impacted by these exclusions. In the event TRIA were allowed to expire, higher prices and reduced availability for terrorism insurance could, within 3 years of expiration, reduce real GDP by an estimated $69 billion and remove 290,000 jobs from the economy.

Clearly, retaining TRIA is a vital component of the country's comprehensive national security plan. It is both reasonable and it is prudent. It is also eminently affordable. Indeed, the cost to the American taxpayer has been effectively zero.

Today, all but the very largest and least likely terrorist attacks would be financed entirely within the private insurance sector. Even in the event of a truly catastrophic attack, TRIA provides the Government with the ability to fully recoup any and all Federal monies outlaid. As a point of fact, from the date of TRIA's enactment in November of 2002 through today, a span of nearly 11 years, the Federal Government and, therefore, taxpayers, have paid nothing, apart from negligible administrative expenses, under the program.

The recent Boston Marathon bombings prove to be an illustrative point. All of the 207 property casualty claims filed in the wake of that event were handled by private insurers who have made payments to policyholders totaling approximately $1.2 million. Not one taxpayer dollar was used to pay any of these claims.

TRIA's structure actually provides at least eight distinct layers of taxpayer protection, as displayed schematically in my Exhibit 4, the Pyramid of Taxpayer Protection.

First is the definition of a terrorist attack itself. It is a very detailed definition and every letter of that definition must be met.

Beyond that, there is a $5 million monetary threshold within the certification. Unless that $5 million threshold is crossed, there will be no certification.

Above that, there is a $100 million triggering event. This means that Federal funds will be paid out only in the event that a terrorist attack produces total insured losses above this threshold.

Then, if we go beyond that, each individual insurer is required to retain losses equal to 20 percent of the premiums earned in lines subject to TRIA.

Beyond that, for losses in excess of that 20 percent insurer threshold, each insurer must retain 15 percent of each dollar beyond that.

And then there is an overall industry threshold of $27.5 billion. Now, for dollars laid out within that $27.5 billion industry threshold, these will—there is a mandatory recoupment mechanism and, in fact, 133 percent of the amount must be collected. And for any amounts above the $27.5 billion threshold, it is at the discretion of the Treasury to collect such funds.

Now, sitting on top of the whole program is a $100 billion hard cap, meaning that beyond that amount, the Federal Government has no responsibility for further losses.

I might also add, there has been an ever-narrowing number of lines covered by TRIA over the years. Back in 2002, approximately 44 percent of the industry's premiums were in TRIA-covered lines. Today, it is approximately 35 percent.

The TRIA also has the effect of reducing taxpayer-funded post-attack disaster aid costs. The fact of the matter is, is if more businesses are covered by TRIA and more workers are covered by TRIA, which they will be as long as TRIA is reauthorized, then that means the demands for post-event disaster aid will be lessened.

So, in summary, there is no question that TRIA has brought much-needed stability and capacity to the market and that it has done so within a fiscally responsible framework. But it is important to emphasize that the majority of the coverage and the capacity in the market today exists only because of TRIA. TRIA's expiration would unquestionably lead to a reduction in capacity with adverse consequences for the broader economy. A larger-scale terrorist attack in the absence of TRIA would effectively take us back to the chaos of the immediate post-9/11 environment.

Thank you for the opportunity to address the Committee today. I would be happy to respond to your questions.

Chairman JOHNSON. Thank you very much for your testimony.

As we begin questions, I will ask the Clerk to put 5 minutes on the clock for each Member.

Dr. Hartwig, some argue that the private sector has developed more capacity to handle terrorism insurance coverage. However, I have seen no research that indicates this unique market can sustain itself without a Government role. Do you believe a Government backstop is still needed, similar to what we currently have in TRIA?

Mr. HARTWIG. There is no question, sir, that a Government backstop is needed to maintain the capacity that is in the market today. As I mentioned at the end of my testimony, as I summarized, all the numbers that you have heard today from each of the witnesses with respect to the amount of capacity that exists in the market exists only because of the existence of the Terrorism Risk Insurance Program itself.

Should that program sunset at the end of 2014, it is absolutely certainly the case that the amount of capacity both among primary insurers and reinsurers becomes significantly constricted. There would still be no interest on the part of capital markets. And, God forbid we were to have an actual large-scale terrorist attack in the absence of the program. We would be back to square one, basically be back at September 12, 2001.

Chairman JOHNSON. Mr. Beshar, what do you think?

Mr. BESHAR. I share Mr. Hartwig's view, Chairman Johnson, that the backstop of TRIA is critical to creating the capacity. I am one of the people who has flagged the fact that the level of capacity has increased in the reinsurance market, but that is predicated on the existence of TRIA. And if you take TRIA away, the strong likelihood is that those property and casualty writers who have the capacity would nonetheless pull back from this peril.

Chairman JOHNSON. Dr. Michel-Kerjan, you have said that, in the past, that a world without TRIA might not necessarily be one with less risk to the Federal Government and the American taxpayers. Can you explain why taxpayers may face more risk and more cost without the program?

Mr. MICHEL-KERJAN. Sure, Mr. Chairman. Well, I think there are two elements, as we have discussed before. Right now, with TRIA, anything that will cost $27.5 billion of injury losses, which will be, by all account, a massive terrorist attack on U.S. soil, will be covered by the private sector for recoupment.

Without TRIA, two things will happen. TRIA not only provides a backstop, but also obliges the insurance companies to actually offer that coverage to all their clients. They do not have to take it, but it is a mandatory requirement. Most likely, if you take out that mandatory requirement, many insurance companies are just going to stop offering that coverage. Proxies are going to increase, especially in the high-risk areas, or what are perceived as high-risk areas—Boston, Washington, New York, Los Angeles, and a few other cities, obviously. The demand for coverage will decrease and the proportion of insured losses will be much higher.

If you do not mind looking at page seven of my written testimony, I mention two things here. The number of Presidential Disaster Declarations is skyrocketing in this country over the past ten, 15 years. We are asking the taxpayers to pay more and more money. That is true for natural disasters and that was true, clearly, during the financial crisis.

To give you one example, 88 percent—88 percent—of the cost of Hurricane Sandy was paid by all of us as American taxpayers. I think we can do better. So if you look at the natural disaster as an example, I think, as I mentioned, it would be very hard for any Congress to deny that relief. As a result, uninsured losses will be much higher. That is why I say that a world without TRIA will actually lead to more exposure to the taxpayers, sir.

Chairman JOHNSON. Dr. Hartwig, would you walk us through the major protections the current program provides taxpayers.

Mr. HARTWIG. Certainly. I referred to an exhibit in my testimony, Exhibit 4, although that may be mislabeled as Exhibit 3 for the second time, titled "The Pyramid of Taxpayer Protection." Basically, I just created this schematic so that it would make it easy to understand that there are at least eight levels of protection for the taxpayer.

And as I mentioned, the very definition of a terrorist attack itself is very detailed and every word of that definition must be met. In addition, the attack must produce at least $5 million in losses before it can be certified.

You have a $100 million threshold before any Federal dollars can be involved whatsoever. Each insurer must then retain 20 percent of loss based on its premiums written in TRIA-subject lines. That can be a very, very large amount of money, hundreds of millions of dollars.

And then, above that, insurers keep skin in the game in every last claim because they are paying 15 percent on every dollar above their individual retention. And then, beyond that, the Government overall, there is a $27.5 billion requirement for the industry overall retention.

That is a large sum of money. So we are starting to get into the sorts of events that rival that of 9/11 itself. If you were to rerun 9/11 today, OK, at the time, $32.5 billion insured loss, pretty much that loss would fall very close to entirely within the private insurance sector itself.

So, for the larger scale losses, the Government has both a mandatory recoupment obligation for some losses and it has the option to recoup every other dollar that it lays out for the truly extraordinarily large losses. And, again, beyond the—an event beyond $100 billion, hard cap, no Government involvement at that point.

Chairman JOHNSON. Senator Crapo.

Senator CRAPO. Thank you, Mr. Chairman.

The current market for terrorism insurance has changed significantly since the program's first creation, and the Marsh report shows that the take-up rates for terrorism insurance rose from 27 percent in 2003 all the way up to over 60 percent in 2012.

Mr. Beshar, your testimony mentions that your company still believes that the insurance market could increase private coverage, thereby reducing taxpayer exposure, and I agree with that assessment. How has the market for terrorism insurance changed and what new sources of funding are available? How can we bring in more private capital?

Mr. BESHAR. Sure, Senator Crapo. I think there are two aspects of that. There is the traditional insurance and reinsurance market, and then there is the world of alternative capital.

On the traditional market, by clarifying aspects like NBCR and perhaps cyber, I think what will happen is, incrementally and gradually, the private market will be able to expand, and that is what you have already seen over the past 12 years and I think that trend will continue.

In the alternative market, which is funds coming in from third-party investors, from hedge funds, even from some pension plans, there are some very intriguing new developments around catastrophe bonds, for example, where countries are now issuing catastrophe bonds to try to protect against specific perils. So the Government of Mexico, for example, has issued a catastrophe bond against earthquake risk. The Government of Turkey has done the same thing to try to mitigate against earthquake risk. And you could envision over the coming years that as people get more comfortable with this risk, that there are some alternative capital providers who may be willing to take it on.

Senator CRAPO. Thank you.

And at the insurance company level, two of the most important figures in the TRIA program are the company deductible and the level of coinsurance. The current deductible is set at 20 percent of its annual direct earned premiums and the level of coinsurance is 15 percent.

Again, Mr. Beshar, you mention potentially increasing the 20 percent level incrementally and possibly bumping up the coinsurance level. Without citing a specific number, is there room to increase both of these levels?

Mr. BESHAR. I think the key question, again, is that capacity has expanded because of the existence of the backstop. So that is why we are strongly in favor of the reauthorization of the program and it is that backstop that is so fundamental. That said, assuming that the trends that have occurred over the past several years continue, and there are not large-scale capacities that reduce the capacity that exists, we do think that there is the ability to expand.

One of the things that the Congress will want to be mindful of is that there are smaller insurers and mutual insurers that are situated differently than the larger insurers, and you want to be sensitive and able to keep them in the marketplace.

Senator CRAPO. Thank you. And, Mr. Kerjan, this question relates to prefunding of the insurance. The United States is not the only country that has developed a public-private partnership to deal with the risk of losses associated with terrorism, and many of these programs require insurers to pay up front for the reinsurance. You, for one, have looked into whether insurers take on greater terrorism risk than they otherwise would because they collect all of the premiums under TRIA but are only responsible for a part of the losses. What impacts would we see if we were to move to a system that involves some kind of a level of prefunding?

Mr. MICHEL-KERJAN. Thank you, Senator Crapo. There are two ways to answer the question. The first one is, if we want more capacity to be provided to the market, the current system has worked pretty well. If we start charging for that Federal backstop, then we cannot have that *ex post* recoupment; the Federal Government is basically covering some of the losses, in return for collecting premiums over time. That is the way the German system, the French system, the Spanish system, and others work.

In the British case, the British Government offers an open line of credit to the Pool Re, which pays for it. If there is another terrorist attack in the U.K., the first five billion pounds will be covered by the private sector through Pool Re, but above that five billion, the British Government is going to open that unlimited line of credit. And the British Government currently receives 10 percent of the premium to provide that line of credit.

So, at the end of the day, it is a matter of what we want to do. Do we want *ex ante* financing or *ex post* financing, and if so, how much do we want the Federal Government to charge for that coverage and what would be a fair premium?

Senator CRAPO. Thank you.

Chairman JOHNSON. Senator Menendez.

Senator MENENDEZ. Thank you, Mr. Chairman.

I would ask that a statement that I have be included in the record.

Chairman JOHNSON. Without objection.

Chairman JOHNSON. Thank you, Mr. Chairman.

And I want to thank the witnesses. This is something that I have been a strong advocate of, because, really, after September 11, we had a disruption in the marketplace, one that was not taken care of by the private marketplace, and, basically, TRIA created market functionality again. And while we would love to see the private sector market fully take care of this, I do not think that, personally, from my perspective, that is still not possible in the world in which we live in.

So I want to ask two specific lines of questioning. One is, terrorism is different from other risks in that it involves intentional human actions that target population centers, infrastructure, economic assets, and it is also harder to predict, in part not only because of the reality that we do not know when individuals will necessarily pursue those intentions, but even to the extent that we are preparing for it, for the possibilities, there is an understandable interest in keeping information about risks and vulnerabilities confidential in order to reduce the chances of an attack and the potential to inflict damage.

So, my question for our witnesses is, how do the differences between terrorism and other risks affect private market capacity to insure against terrorism risk, and to the extent that these differences translate to higher costs or reduced availability of insurance against terrorism risk, what are some of the broader consequences for our economy and our society? I welcome anyone's answers. We can go down the line.

Mr. HARTWIG. I think we might all comment.

Senator MENENDEZ. All right. So, go down the line.

Mr. BESHAR. Senator Menendez, I will start, perhaps focusing on workers' compensation cover, what would be the potential impact. It is an unusual line of cover in that employers like Marsh and McLennan are required to obtain the cover to protect their employees and carriers are required to provide the coverage without regard to what the cause of the loss is, whether it is an act of war, an act of terror, arson, whatever is the risk.

And what we are seeing potentially in the marketplace is that workers' compensation carriers are beginning to pull back, those who provide coverage to large amounts of individuals concentrated in areas in New Jersey, in the metropolitan New York area, Chicago, L.A., Washington. And so the TRIA backstop is critical to inducing those workers' compensation carriers to, in fact, provide that cover. And if it is not there, if it becomes much more expensive to get workers' compensation coverage, we are concerned that that has a negative drag on economic growth and job creation.

Mr. HARTWIG. If I could add on to what Mr. Beshar said, workers' comp is really just sort of the beginning of the issue here. When it comes to terrorism risk, insurers face a unique form of aggregation problem here. Typically, when we think about a large-scale natural disaster like a hurricane, for example, you are talking about mainly your damage associated with wind. It is a property type of damage, business interruption loss. But you do not have large-scale loss of life such as you had in 9/11.

So, with respect to terrorism, particularly in the absence of a Terrorism Risk Insurance Program, you have insurers modeling in a way that they do not normally have to model for a major catastrophic loss. They are looking not only at the possibility of extraordinarily large property damage and business interruption losses, but they are looking at potentially multi-billion-dollar losses with respect to workers' compensation. So you have got this layer—it is basically many more layers than you would have for more traditional losses.

That makes the modeling much more difficult, and what it also does is, in effect, requires an insurer to take, say, a map of the areas in which it operates, ascertain literally how many dollars it has in risk, not just in terms of insured structures but insured lives with respect to workers' comp exposure and other types of coverage, and it cannot exceed a certain amount in each one of those areas. So it makes it much more difficult to model and makes the whole insurance program that it must orchestrate much more difficult.

Senator MENENDEZ. Well, let me go through another line, if I may, and I am happy to entertain your answer, as well, but I just want to, in the time that I have left.

Mr. Beshar, in your 2013 Terrorism Risk Insurance Report, you predict that without a Federal backstop, the cost of terrorism insurance would rise for areas with concentrations of people or economic assets, infrastructure such as transportation, pipelines, and other elements. I think of my region that Senator Schumer and I share, just as one example. In a two-mile stretch, just a simple two-mile stretch of my State, we have the largest container port on the East Coast, the megaport of the East Coast; we have one of the largest and busiest airports in the country at Newark International; we have rail lines, Amtrak, New Jersey Transit, and others, and PATH, that carry hundreds of thousands of people back and forth each day to work; and critical industrial infrastructure and the most dangerous two miles in America because of the Chemical Coastline.

So, while that is a regional reality, the consequences, though, of such an attack are broader to the national economy, would not that be a fair comment?

Mr. HARTWIG. Absolutely, Senator Menendez.

Senator MENENDEZ. Yes. OK.

Mr. MICHEL-KERJAN. Let me just add, I think that the discussion has been mainly about insurance. Ultimately terrorism is a national security issue, and as any government around the world, the question is, how do we create a mechanism that will help the country bounce back after a disaster? And insurance is one way to do it, an effective way to do it.

So let us not see terrorism as something that insurance companies have to cover. They do not have to cover it. We made that a mandatory offer. We, the country. That has been a national decision. I think that is the most effective way to actually cover the risk and all the claims. We have other programs in this country that do not necessarily rely on the private insurance sector which I think we should learn from, some failures, as well, so——

Senator MENENDEZ. Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Reed.

Senator REED. Well, thank you very much, Mr. Chairman, and let me echo the comments of the Professor.

Risk insurance is a national security issue as well as a banking issue, and I have the privilege of serving on the Armed Services Committee as well as this Committee and we have seen that there are still significant threats. In fact, tragically this week in Kenya, it was a commercial property that was attacked, and not only was there great loss of life, but destruction of the property.

So the issue, as it was after 9/11, remains today. How do we maintain a viable commercial real estate sector in our economy given this persistent threat of terrorism and given the role of the Federal Government in preempting it, preventing it, and if it happens, to be able to help absorb the risk? So I think it is absolutely essential that we have to extend the reinsurance program going forward.

We have to keep markets open. We have to also, I think, keep, in fact, to continue our growth, to remove impediments to potential investment, particularly in large commercial projects. Without Terrorism Risk Insurance, there is an impediment. There is a certain calculated cost that the developer has to bear if it is not there. And I think the way it is designed, with the first losses going to the private sector and only in extreme cases the Federal sector stepping up or the national sector, makes some sense.

But let me just begin with a question and ask all of you, beginning with Mr. Beshar, there is a presumption here if we take away this legislation, the private capital markets have a viable alternative to TRIA. Is that the case, in your view, Mr. Beshar?

Mr. BESHAR. We do not believe so, Senator Reed. We think it is that backstop that has created the market and created the capacity. And so if you take that backstop away, we think the market capacity will shrink quite significantly.

And to your point about kind of where the potential targets are, one of the things that was most striking to us about the Marsh report was that the take-up rates are really across the country and across industry, including Rhode Island, that there is a perception that if you are hosting a sporting event, for example, you know, the NFL and the NBA, the NHL, everybody recognizes that there is a risk that is not concentrated just in the large urban areas of the United States.

Senator REED. That is a very good point.

Professor, your comments.

Mr. MICHEL-KERJAN. No, I think I would agree with Mr. Beshar. I think we have reached a point where almost everybody agreed that it has been a great program. I think that our discussion today has been more about how we transform that program incrementally, so that we increase the market's capacity to absorb more risk.

Let me also say that a lot of the discussion has been about where the market is today, where it could be in the next few years. All of that is important, but I think the big question is what will happen to the market in the aftermath of a terrorist attack, a large terrorist attack, whether it is outside the U.S., as we have seen in 2005 in London, or elsewhere. I think having that Federal backstop reassures the insurance industry that, for catastrophic risk, none of them will go under, and I think that is a very important statement to make and an important aspect to keep in mind.

We know from natural disasters that the market tends to be highly volatile after a big natural disaster. I believe with that Federal backstop, actually, that market will remain pretty stable after an attack, which I think is a win-win situation we are all looking for.

Senator REED. Thank you.

Mr. Hartwig, you have a comment.

Mr. HARTWIG. Thank you. And just quickly, and to echo what some of my fellow witnesses have said, absolutely. There is no question that is what has happened in the 11 years since TRIA has been in place. And while this was not by the original design, we have found that TRIA is an essential part of this country's national security plan, and I think I have heard you mention that, sir. And so in the absence of TRIA, we wind up creating a gaping hole in that plan.

And as we just heard Professor Michel-Kerjan say, that if we wind up in a situation where TRIA has expired and we have a large-scale terrorist attack or even something along the lines of what we saw in Nairobi, Kenya, which could be easily copycatted here in the United States, perhaps not just at one location but in several locations simultaneously, you wind up, I think, with a large-scale loss of confidence in the market.

Now, when we look at every other segment of the financial services industry, there are contingency plans for dealing with catastrophes of every sort. When it comes to a terrorism loss, this is part of our national security plan. It is part of what is absolutely integral to businesses all across the country today, and not just Rhode Island, but from coast to coast.

Senator REED. Well, thank you very much.

Just a final thought, and that is as we go forward, there is another dimension to terror attacks that really was not so obvious in 9/11, and that is cyber security. I do not know, and I think we have to think carefully about how we would incorporate or would we incorporate aspects of that in any type of legislation, but that is just food for additional thought.

Thank you, Mr. Chairman.

Chairman JOHNSON. Senator Tester.

Senator TESTER. Thank you, Mr. Chairman and Ranking Member Crapo.

I want to start with a question that Senator Crapo talked about and that is potentially raising the deductible, and I am sure there probably will be some proposals to do exactly that. Could all of you or at least a couple of you talk about the impact of raising the deductible on some of the small or mid-sized and even some of the large insurance companies who are currently underwriting terrorism insurance? You can go ahead.

Mr. BESHAR. Bob, do you want to start?

Mr. HARTWIG. Sure. I will start, and I think it is appropriate, Senator, to sort of divide the discussion up between some of the larger companies and some of the smaller companies.

Senator TESTER. Yes.

Mr. HARTWIG. Just in practice, the way that an insurance company operates is that we are a very conservative industry. We do not operate on the edge. We do not operate to the very last dime of capital in our books. That is why this industry is absolutely rock solid after a decade of record catastrophe losses, and, quite frankly, we have every intention of staying that way and TRIA is absolutely essential to that.

So, I know that there will be a discussion about raising retentions and deductibles and so forth, but raising deductibles and retentions in and of themselves does not create capacity, OK. What creates capacity, as insurers learn more about this market or external events influence the relative riskiness of operating this space at any level of dollars at risk.

So, to the extent that we do not have a major terrorist attack, that helps to increase confidence. To the extent that there are advances in modeling terrorism risk, that helps reduce uncertainty and create confidence.

Has there been some growth——

Senator TESTER. I have got you. I want to know what the impacts on small and mid-sized companies are if we increase the deductible.

Mr. HARTWIG. On small—are you referring to——

Senator TESTER. Small, mid-sized, and large reinsurers. I want to know what the impact is going to be on them, positive, negative—I understand about growth and increasing capacity.

Mr. HARTWIG. Right.

Senator TESTER. But that is not my question.

Mr. HARTWIG. Right. With respect to smaller insurers, it would likely be a negative——

Senator TESTER. OK.

Mr. HARTWIG.——because they are not——

Senator TESTER. How about mid-sized folks?

Mr. HARTWIG. They may have a little more room, but in the United States, when we are talking about mid-size companies, we are talking about regional, super-regional companies——

Senator TESTER. Right.

Mr. HARTWIG. I think it is still an issue. Larger companies have a little bit more opportunity there. On the reinsurance side, it is a little less clear.

Senator TESTER. Thank you very much.

So, if we did that, and I do not want to put words in your mouth, it would potentially reduce competition in that marketplace, if the small companies were to go by the wayside?

Mr. HARTWIG. I do not think that you wind up increasing competition, let me put it that way.

Senator TESTER. OK. All right. Sounds good.

I was curious to know—and this is for Mr. Beshar—can you speak specifically about the role TRIA would play in rural areas, where we do not have the big stadiums, you do not have the big casinos, kind of what do we need to be looking out for in rural America and how TRIA would impact them.

Mr. BESHAR. Absolutely, Senator. So, again, in terms of what we took away from the report, we were struck at how broad-scale the take-up rates are across the regions and across the industries.

Senator TESTER. Yes.

Mr. BESHAR. To be sure, we were polling our clients. Our clients tend to be larger companies and mid-size companies, as the Professor identified. And so part of the objective is not just to be protective of smaller companies, for example, to create more capacity. Pricing comes down as there is more capacity, and then smaller companies, like those, perhaps, that were impacted by the bombing in Boston, are able to get access to cover. And similarly, I think, smaller rural areas would then follow along with that, where coverage becomes more viable and more relevant to them.

Senator TESTER. OK. I think in your testimony, Dr. Michel-Kerjan, you talked about a lack of knowledge about—and I do not want to put words in your mouth—about the penetration in small businesses. Is there anything that we can do about that to find out——

Mr. MICHEL-KERJAN. Sure, and I think that is an important question. We know a lot about large corporations, thanks to Marsh and McLennan and AON, to some extent, but that is about it. We know almost nothing on small businesses.

Mr. BESHAR. Really, just Marsh and McLennan there. Yes.

[Laughter.]

Mr. MICHEL-KERJAN. That is about it. Let us be serious. We do not know much about other markets. So, yes, I mean, we could think about the GAO being asked by Congress to actually do a market study on small businesses across the country. There could be surveys realized. Today, beyond that, we know almost nothing. We hear that some small businesses buy it. Other businesses actually get it for free.

Senator TESTER. Yes.

Mr. MICHEL-KERJAN. We do not know anything.

Senator TESTER. OK. My last question is for Dr. Hartwig. Mr. Beshar brought up the fact that cyber should be a part of TRIA. I looked at the definition. It looks to be able to encompass that. I wanted to know your opinion.

Mr. HARTWIG. Yes. I would concur, and that under most instances of a cyber attack, that would perhaps, for instance, cause an explosion at a power plant or some such thing, that type of loss would be covered so long as it met the definition of a terrorist attack. So, in most cases, yes.

Senator TESTER. OK. Thank you all very much for your testimony. Thank you for your time.

Chairman JOHNSON. Senator Manchin.

Senator MANCHIN. Thank you very much.

I just have a couple questions. Unlike other instances of Government-offered insurance, I have been told that TRIA has cost taxpayers next to nothing as far as since the Treasury covers 133 percent of its payments from insurers in the years following initial loss. On the other hand, TRIA has helped commercial real estate developers to receive financing for construction projects. I also understand that has helped them immensely.

And my question would be, would TRIA cost taxpayers money in the future by your predictions, and what would happen to small community-based developers if TRIA was no longer available? I know you have touched on different things of it, but this is a pretty important aspect for the economy, right?

Mr. HARTWIG. Right, and we may all have some comments on this, but certainly, there is no question that in the absence of TRIA, it would cost the economy——

Senator MANCHIN. There is nothing else on the marketplace.

Mr. HARTWIG. For terror coverage, no, other than internalizing the loss and assuming the loss on your own. No. There is nothing else out there.

Senator MANCHIN. There are no insurance companies that—if this goes away, there are no insurance companies or the insurance industry willing to step to the plate.

Mr. HARTWIG. There would be a reduced amount of capacity, a drastically reduced amount of capacity in the marketplace.

Senator MANCHIN. Doctor?

Mr. MICHEL-KERJAN. No, I think there will still be some coverage. The question is, at what price?

Senator MANCHIN. We are going to have, and I think that both the Chairman and Ranking Member will say on the floor, with our full membership, some people will say, why should Government be involved? Does Government even need to be involved? And that is what we always—there is a place for Government, especially when it can shore up a market and improve the economy, the economic situation, without costing the taxpayers, and this is one, it seems to me, makes sense. But if I am missing something, please tell me.

Mr. BESHAR. Senator Manchin, we agree powerfully with what you have said, that this has been a model program and that when Congress has reauthorized it in 2005 and 2007, they have made it better. They have modernized it. The recoupment——

Senator MANCHIN. Not been a burden on the taxpayers in any way, shape, or form that you can see?

Mr. BESHAR. That is correct.

Senator MANCHIN. We have not found any of that. If that is the case, if there is a profit to be made, why would the private sector not—I am being the devil's advocate—why would you not let the private sector take it over? Why would the Government have to be involved, if it has been such a good program?

Mr. MICHEL-KERJAN. Well, let me say that right now, it is not just a Federal program. The first $27 billion would be paid by the private sector, and that is important to keep in mind. And for any event to cause $27 billion of injury losses will have to be a massive terrorist attack. So, it is not just a free fare program starting at zero dollars. That kicks in at $27 billion, which is very significant.

Senator MANCHIN. OK.

Mr. HARTWIG. And if I might add to that, in the absence of TRIA and we have a large-scale terrorist attack, the Government is going to be called to act. There are going to be——

Senator MANCHIN. Whether there is insurance or not——

Mr. HARTWIG. Right. Exactly.

Senator MANCHIN.——the Government is going to step to the plate.

Mr. HARTWIG. In the absence of insurance, I can guarantee you the Governors from the affected States will be here and will be asking for very, very large sums of money from the Federal Government.

Senator MANCHIN. So, any naysayers against this program——

Mr. HARTWIG. Right.

Senator MANCHIN.——we are basically, you are going to pay me now or pay me later.

Mr. HARTWIG. That is exactly the point, Senator, that one way or another, you could work with the private sector, who will internalize most of these losses under the vast majority of scenarios, including the very large events that are nearly $30 billion, or nearly the entire burden could be placed on the Federal Government after the fact, and the Federal Government has, I might also add, has no means for effectively managing these types of claims. These claims will be managed in the private sector in an efficient manner——

Senator MANCHIN. Let me just say this——

Mr. HARTWIG.——not only financed, but managed.

Senator MANCHIN. They give us a little bit of time here, so I have got to be quick.

The thing that would be—if we have a massive hit and a massive loss, under TRIA, still, the Government will be paid back eventually, correct?

Mr. HARTWIG. Paid back and then some.

Senator MANCHIN. A hundred-and-thirty-three. Right. If it goes away and the market does not pick it up and we have a massive hit, then it is basically out of the taxpayers' pocket and no reimbursement whatsoever.

Mr. HARTWIG. Correct.

Senator MANCHIN. OK. Next of all, how long should this reauthorization be and should we include the Secretary of Homeland Security in the terrorism certification process? Should they be involved in that? And how long should this one be that we are working on right now?

Mr. BESHAR. Personally, I think it is a very sound idea to have the Secretary of Homeland Security as a participant, together with the Secretary of the Treasury, the Secretary of State, and the Attorney General. Our view is that Congress has improved this program over time, and so you are trying to strike that balance between consistency and——

Senator MANCHIN. It has changed every time we have done it, so——

Mr. BESHAR.——so we advocate——

Senator MANCHIN.——we have not found the sweet spot yet.

Mr. BESHAR. Indeed. We advocate a 10-year reauthorization.

Senator MANCHIN. Ten year?

Mr. BESHAR. Yes.

Senator MANCHIN. Do all of you agree?

Mr. HARTWIG. Certainly, a long-term renewal is what——

Senator MANCHIN. Well, that does not work well here. Give us a number, because——

[Laughter.]

Mr. HARTWIG. Can I start with permanent? Is that—permanent would——

Senator MANCHIN. Permanent is probably a more appropriate way to go, then you go down to a 10-year minimum?

Mr. HARTWIG. Right.

Senator MANCHIN. Is that where you would be? You all think 10 years should be the minimum we consider, right, so we do not——

[Witnesses nodding heads.]

Senator MANCHIN. OK. Thank you. It is very interesting.

Chairman JOHNSON. Senator Schumer.

Senator SCHUMER. Thank you. Thank you, Mr. Chairman, Ranking Member, witnesses, for holding this hearing. It is very important, obviously, to the country and particularly to New York and very important to me, so I appreciate doing this way in advance, because we have got to make progress on this issue, even though the program does not expire until the end of 2014.

As we all know, policies get written much more quickly than that, and if we wait until the last minute, there will be billions of dollars of real estate that does not go in the ground because people are uncertain whether they can get terrorism insurance or they are uncertain whether they can get a mortgage, so they are uncertain whether to plan a building, *et cetera.*

So, the sooner we do this, the better, and we are reminded by events near and far—the Boston Marathon bombings, brutal attacks at the Westgate Mall in Nairobi—the threat of terrorism is ever with us. The idea that, well, 5 years after 9/11, we could forget about terrorism, everyone knows that is not true. Well, it goes hand-in-hand. We cannot forget about terrorism insurance, either, because the specter of terrorism can hurt economic growth and economic growth is what we want.

We know, for instance, the Kenyan mall massacre reminds us that Government buildings and skyscrapers in Manhattan or Los Angeles or Chicago are not the only potential targets. There are shopping malls and sports stadiums and factories and airports all over the country, all of which can be impacted if terrorism insurance is not available.

So, as a New Yorker, the rebuilding of downtown in the years following 9/11 has been nothing short of a miracle. It is a more vibrant neighborhood now than it was before 9/11, and in part, that is because of the TRIA program. And all those jobs that were created, homes that were created, wealth that was created, in part, is because of TRIA. So, I hope we will work with you, Mr. Chairman, and Ranking Member Crapo to extend the program as quickly as we can.

So, here are my questions. First, Mr. Beshar, in your testimony and in Marsh's report, you indicate that the average take-up rate for terrorism insurance is at least 53 percent in every region of the country, and, of course, much higher in certain regions. Take-up rates for several major industries—media, telecom, education, transportation—range from 66 percent to over 80 percent. How does that compare to most other types of insurance and what does this tell you?

Mr. BESHAR. I think we have been surprised, Senator Schumer, at how strong the interest in this cover has been. We assumed, perhaps like you, that it would be much more concentrated in the Northeast, but in fact, the rates in the West, as Senator Heller mentioned previously, have been very strong. Take-up rates for institutions like nonprofits and educational foundations have been much stronger than we would have anticipated. So, really, across the board, there is profound interest in this cover.

You mentioned real estate developers. Many mortgage—many lenders require as part of providing a mortgage that there is terrorism cover that the developer has obtained, and if TRIA is not available, the pricing for that cover, if it is available, will go up significantly.

Senator SCHUMER. Thank you.

OK. You are all insurance and risk management experts to one degree or another, and if you had been asked last week to evaluate the risk of an attack on the Westgate Mall in Nairobi, would you have been able to evaluate it? And a related question. Is not one of the difficulties in making such determinations that the necessary information is difficult, in some cases impossible, for the private sector to obtain because it is classified national security information that we would not want out there for the world to see? Whoever would like to take it. Dr. Hartwig.

Mr. HARTWIG. Yes, sir. As a fellow New Yorker, I share with you the sentiments about the city. Every day on my way to work, I go past the Ground Zero site and I am reminded every day about the benefits of TRIA, believe me, in a very firsthand way, as Mr. Beshar's company is, as well.

But to answer your question directly, the likelihood of something like in the Westgate Mall in Nairobi, Kenya, happening here, 10 years ago, basically, I said it was a matter of when, not if, it would happen. Thank God, it has not happened, something of that magnitude. But we have had the Boston Marathon attack this year.

It is also incorrect to say that the Boston Marathon is the only event, in some sense, that has occurred. We have been very lucky with interdiction, thank goodness, to the resources at the Federal level and at the State and in the city of New York itself. But there have been several plots. The only reason they did not actually happen was because of the ineptitude of the attacker himself, individuals such as the Underwear Bomber, for example, the Shoe Bomber, or an individual trying to blow up a bomb in Times Square.

So, the reality is that I still think it is a matter of when, not if, for a Westgate Mall-type incident here in the United States, and absolutely, it is very, very difficult to obtain information, certainly if you are an insurer, and it is even difficult for the country's national security agencies to obtain this information. It is far more difficult for insurers to obtain this sort of information, which is inherently why it is difficult to model these sorts of events.

Senator SCHUMER. Right. OK.

Let me ask one final question, and this, again, can go to any of the witnesses who wishes, and it is my last one, with your permission, Mr. Chair. With many types of insurance, there are things the insured can do to reduce the risk of loss. Flood insurance, raise the level of your house or build a dune or a structure in front of your house. In the case of terrorism, what can commercial real estate developers or owners of malls or sports stadiums do to mitigate the potential risk of terrorist attack, and is it not one of the challenges here that terrorists will actively seek to overcome whatever defenses that you have planned? Do you want to take that, Dr. Kerjan?

Mr. MICHEL-KERJAN. Let me take it. You summarized this very well, what we are facing here. Whether it is flood or earthquake, we know what the engineering solution should be. Many people do not do it, but that is another issue.

With terrorism, well, to take 9/11, it would have been very hard for any commercial entities in the World Trade Center Towers to do anything to prevent a commercial aircraft crash against the building.

So, to your question, I think the answer is near to zero in terms of what can we do to prevent these attacks as a commercial entity. You can have more cameras. You can have more physical protection, and in New York afterwards, you see that happening. That is part of a broader national security response to the threat of terrorism. But I think there are only a few things that a commercial entity can do, and if you move from New York to other parts of the country, and maybe at the lower level of revenue, many of these companies do not have the means to actually invest in protective measures, and even if they do, well-organized, informed terrorist organizations will just select the other target which is less protected. So it is a dynamic uncertainty, and I think that is very peculiar to terrorism threats.

Senator SCHUMER. Thank you, Mr. Chairman.

Chairman JOHNSON. Thank you, again, for all of our witnesses for being here with us today.

I look forward to working with all of my colleagues on the Committee to move a bill to extend the Terrorism Risk Insurance Act as soon as we can.

This hearing is adjourned.

[Whereupon, at 11:12 a.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF SENATOR TIM JOHNSON

Good morning, I call this hearing to order.

Two weeks ago, we observed the 12th anniversary of the tragic September 11th terrorist attacks on our country. In the aftermath of the tragedy and after suffering steep losses, insurance companies stopped offering terrorism coverage as part of their commercial property policies. This had a destabilizing impact on various parts of our economy.

Congress responded by creating the Terrorism Risk Insurance Program to provide a narrow and targeted Government backstop for this insurance coverage. The program proved helpful, creating certainty for many businesses, including developers, construction companies, commercial lenders, as well as private insurance markets.

The program has since been reauthorized by Congress twice. The last time, Congress made very few changes and extended the program for 7 years. It is my hope that once again we will be able to find bipartisan consensus for the reauthorization of TRIA well before the program expires at the end of 2014.

While a few may seek dramatic changes or even try to eliminate the program, we should remember that taxpayers have not lost any money on the program. The program's unique structure has fully protected taxpayers while promoting economic growth by preventing interruptions in insurance coverage and providing certainty for commercial property developers working on stadiums, universities, malls and other projects across the country.

Today, we review the state of the terrorism risk insurance market, and I look forward to hearing from our witnesses about how the current program has functioned and the ongoing need for the same limited Government backstop we already have in TRIA.

With that, I turn to Ranking Member Crapo for his opening statement.

PREPARED STATEMENT OF SENATOR ROBERT MENENDEZ

Thank you, Mr. Chairman, for holding this hearing today on the critical issue of terrorism risk insurance. Although TRIA does not expire until next year, it is important for this Committee to start working on reauthorization now, to give greater certainty to the market as insurance policies start coming up for renewal.

Congress first enacted the Terrorism Risk Insurance Act in 2002, when, after the terrorist attacks of September 11, 2001, we saw a total breakdown in the market for insurance against terrorism risk. Many insurers stopped offering coverage entirely or made it available only at very high costs. Businesses, as a result, faced the prospect of dramatically higher costs or an inability to get financing to invest, create jobs, and build new facilities. Congress responded by enacting TRIA, which provides a limited Federal reinsurance backstop that restored market functionality, and since then we have twice extended the program.

In my State of New Jersey, we are acutely aware of the challenges that TRIA addresses. The very things that make us strong economically and enrich our lives culturally also make us most vulnerable. In just a two-mile stretch of my State, we have the largest container port on the East Coast, one of the busiest airports in the country, rail lines that carry hundreds of thousands of people back and forth to work every day, and critical industrial infrastructure. Not to mention high population density, important cultural centers and landmarks, and major highways.

New Jersey is an example, but the problem is national, and affects economic and cultural centers and infrastructure in every State. So I am pleased that the Committee is starting the work of reauthorization and I look forward to hearing from our witnesses today.

PREPARED STATEMENT OF SENATOR MARK R. WARNER

The Terrorism Risk Insurance Act expires at the end of 2014. As someone who is passionate about infrastructure investment and rebuilding our economy, I care deeply about the reauthorization of this program.

Some of our colleagues in the House would like to let TRIA expire. They view the program as an "inappropriate" Government subsidy. Never mind the facts, which are that not one dime of taxpayer money has been lost through this program since its inception.

Next, they assert that the insurance industry can adequately cover losses from terrorism. This ignores a stark reality demonstrated by the insurance industry in the aftermath of 9/11, which immediately refused to write new policies covering terrorist acts. Such a situation is not surprising—unlike for natural disasters, where the industry is aided by meteorological data and historical analysis, it is impossible to predict terrorism. Insurance companies certainly do not have access to information our intelligence agencies possess.

Some critics see TRIA as a subsidy for New York City. Unfortunately, as the events of last April's Boston marathon tragically demonstrated, terrorism can strike anywhere in our Nation. An expiration of TRIA will leave landmarks in every State of the country vulnerable. Each senator represents major commercial real estate developments, sports arenas, entertainment plazas, and college campuses that are potential targets. It would be a disaster to leave our States' facilities without coverage.

Without reauthorization the country risks a freeze in commercial real estate development, as insurers will be unable to appropriately price risk and may thus exit the market. It will also impede our Nation's nascent economic recovery by creating uncertainty.

Commercial leases and construction projects depend on having appropriate insurance coverage. To avoid additional uncertainty, I believe we should reauthorize TRIA on a long-term basis.

I thank Chairman Johnson and Ranking Member Crapo for holding this critical hearing, and I look forward to working with them both to move legislation expeditiously.

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COMPANIES

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Testimony of

Peter J. Beshar

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Marsh & McLennan Companies

Before the United States Senate
Committee on Banking, Housing and Urban Affairs

Reauthorizing TRIA: The State of the Terrorism Risk Insurance Market

September 25, 2013

Washington, DC

Introduction

Good morning Chairman Johnson, Ranking Member Crapo, and members of the Committee. My name is Peter Beshar, and I serve as Executive Vice President and General Counsel of Marsh & McLennan Companies. I would like to thank you for the opportunity to share our perspective on the Terrorism Risk Insurance Act.

Terrorism is a deeply personal topic for Marsh & McLennan Companies. In the September 2001 attack on the World Trade Centers in New York, our Company lost 295 employees and scores of other business associates. Indeed, together with the NYC Port Authority and Cantor Fitzgerald, we lost more employees than any other institution in New York.

Our Company also has a unique perspective on the terrorism insurance market. Through our market-leading brands — Marsh, Guy Carpenter, Mercer, and Oliver Wyman — our 54,000 colleagues in more than 100 countries advise clients on the key issues of risk, strategy, and human capital. While Marsh & McLennan Companies is not an insurer, the Company, through Marsh and Guy Carpenter, supplies analytics and provides intermediary services to all the parties involved in the placement of terrorism coverage, from the buyers and sellers of terrorism insurance to the key reinsurers in the market.

We consider TRIA to be a model of a public-private partnership. TRIA restored insurance capacity at a critical time after 9-11 and has been important in fostering a well-functioning terrorism insurance market since that time. In 2005 and again in 2007, Congress adopted sensible reforms that appropriately expanded the role of the private insurance market and reduced the exposure of the federal government. Thankfully, thus far, the federal government has not made any payments under TRIA. The only federal appropriations associated with the program have been for its administration.

We strongly endorse the reauthorization and modernization of the TRIA program.

There are four core points that I would like to make:

First, I will summarize key highlights from Marsh's "2013 Terrorism Risk Insurance Report," which was released in April on Capitol Hill (Appendix A). It will help you gain a sense of the current state of the US market for terrorism insurance coverage, including pricing, availability, and the private sector's capacity to offer coverage absent a federal backstop.

Second, I will describe the current levels of surplus capital in the reinsurance market to help you assess the areas (1) where the private market can play a greater role and (2) where TRIA remains a critical necessity.

Third, I present Marsh & McLennan Companies' recommendations for reform related to nuclear, biological, chemical and radiological (NBCR) attacks, cyber terrorism, and the TRIA certification process.

Fourth and finally, I frame the debate over additional reforms that third-party groups have suggested and identify two important risks that may occur if TRIA is not renewed.

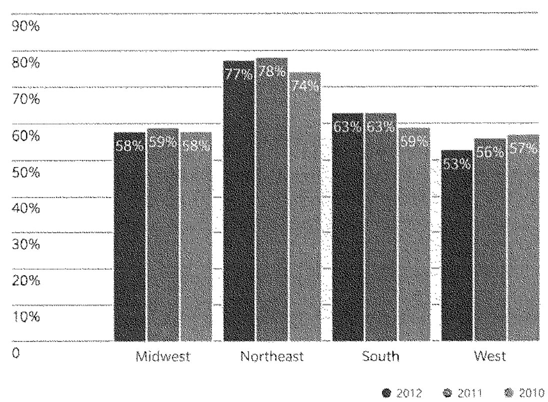
1. Highlights of the Marsh Terrorism Risk Insurance Report

The Company's April 2013 report, the only survey of its kind, sampled nearly 2,600 Marsh clients across the US. The report examined purchasing patterns for 17 industry sectors by region and examined take up and premium rates. It confirms that TRIA's "make available" provision has helped foster a robust private terrorism insurance market. The top-line findings from Marsh's report include:

Take Up Rates by Region

- The take up rate for terrorism insurance is over 55% in every region of the country. In the South. In the Midwest. Indeed, take up rates have grown consistently in the West. Thus, this is not simply a Northeast phenomenon.

Figure 1: Region Take Up Rates

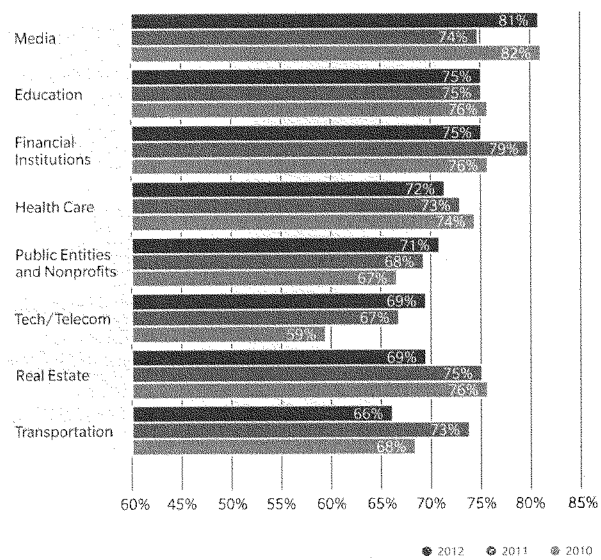


Take Up Rates by Industry Sector

- Both private and public institutions are active buyers of terrorism coverage. Media companies, real estate firms, and education institutions all have take up rates over 75%. Interestingly, public entities and non-profits are increasingly turning to terrorism insurance.

- Larger companies are more likely to purchase property terrorism insurance and receive lower rates on line as a percentage of overall property premiums.

Figure 2: Industry Take Up Rates



Other Findings

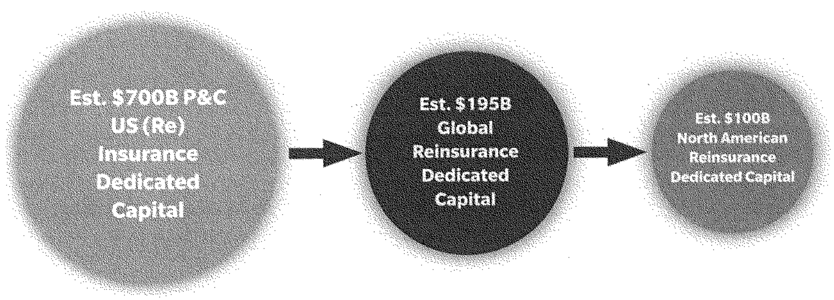
- Among US captive insurers managed by Marsh, 25% underwrite at least one TRIA-specific program. Additionally, hundreds of owners of captives provide some element of terrorism coverage.

- TRIA's expiration or substantial modification in the future will almost certainly affect existing TRIA coverage, standalone terrorism pricing, and TRIA captive programs. In particular, terrorism insurance capacity may be difficult to acquire for insureds with significant exposures in a central business district of a major city. In addition, the absence of, or a serious modification to TRIA, could severely impact the workers' compensation market.

2. The Current Capital Position of the Reinsurance Industry

Guy Carpenter, our leading reinsurance intermediary, recently presented its mid-year report on the reinsurance market and found that global deployed reinsurance capital[1] grew from $178B at the end of 2011 to $195B at the end of the second quarter of 2013.[2] By comparison, this figure was less than $160B in 2007.

Figure 3: Guy Carpenter Analysis of Dedicated Insurance and Reinsurance Capital



[1] Insurance capital is equity of shareholders of a stock insurance company. The company's capital and surplus are measured by the difference between its assets minus its liabilities.
[2] "Capital Stewardship: Charting the Course to Profitable Growth": http://www.guycarp.com/content/dam/guycarp/en/documents/dynamic-content/Mid-Year-Market-Overview-Sept-2013.pdf

It is important to note, however, that not all capital is dedicated to or capable of writing terrorism coverage. While alternative, or "capital markets," providers have brought substantial reinsurance capacity into the industry, most have little to no appetite for the peril. Some are forced to decline on the basis of legal obligations made to their investors, whereas others simply avoid the exposure on the grounds of correlations with financial markets risk.

Nonetheless, were capital trends to continue and Congress to adhere to the precedent of decreasing federal involvement in terrorism insurance, Marsh & McLennan Companies believes that the insurance market could increase private coverage, thereby reducing taxpayer exposure. That said, there are limitations to what the market can absorb in losses, particularly in the event of a large-scale conventional attack or a NBCR event. For example, a reputable third party vendor modeled the estimated impact of a 10-ton truck bomb explosion in Manhattan causing $38.6B in workers' compensation and property damage. Moreover, a nuclear bomb detonated in the Manhattan central business district would have a modeled loss estimated at $941B. In our judgment, a federal backstop is necessary to protect against these types of catastrophic events.

3. Marsh & McLennan Companies' Recommendations for Reform

TRIA has been, in our view, a model example of what a public-private partnership should be. TRIA's "make available" provision, in return for the explicit federal backstop, restored insurance capacity at a critical time after 9-11. Since then, Congress has implemented reforms that have expanded the private terrorism insurance market as the industry has recovered. We offer three recommendations for further refining and modernizing the TRIA program, which should be reauthorized for a minimum of 10 years.

NBCR Coverage – Marsh & McLennan Companies recommends that Congress specifically clarify during the reauthorization process that coverage should be provided by TRIA for all forms of terrorism (i.e., conventional and NBCR) if coverage is afforded on the primary policy. For instance, there is ambiguity in the market currently as to whether TRIA covers workers' compensation in the event of an NBCR-related act. In fact, a leading rating agency recently stated that NBCR related events remain outside of TRIA coverage. It is Marsh & McLennan Companies' view that TRIA would cover workers' compensation losses if a certified NBCR event occurred.[3]

[3]Fitch Ratings' Report: "U.S. Terrorism Reinsurance: Looming Uncertainty of Program Renewal": http://www.insureagainstterrorism.org/FitchReport-8-13.pdf, see page 3.

Cyber Terrorism – Former Secretary of Homeland Security, Janet Napolitano, cautioned in her farewell address: "Our country will, at some point, face a major cyber event that will have a serious effect on our lives, our economy, and the everyday functioning of our society."

This is a potentially new form of terrorism, which did not credibly exist at the time of the last reauthorization in 2007. Whether it is one or a series of cyber attacks, the impact of a "cyber 9-11" could be crippling, particularly if the attack were directed at one or several of the nation's critical infrastructures such as our telecommunications networks, food and water supplies, or health care institutions. Currently, there is uncertainty if TRIA would cover an act of cyber terrorism that resulted in catastrophic loss. There is not clear language in the law that states unambiguously that cyber terrorism would fall within the scope of TRIA; we, therefore, recommend that Congress analyze the best way to address this new terrorism risk in the reauthorization of the TRIA program.

Clarify Certification Process – Currently, TRIA enumerates specific requirements for an act to be certified as terrorism under the program.[4] However, the process by which an act of terrorism is certified remains uncertain, and there is not a mandated timeline for determining an event's certification. As an example, the federal government has neither certified the April 2013 Boston bombings as a terrorist event, nor has it offered a timeline to do so. This creates uncertainty for insureds and insurers alike. For instance, without certification, there may be delays in indemnity payments under private property or business insurance to business owners, which could jeopardize their financial position and ability to resume business operations. Marsh & McLennan Companies recommends that Congress include language in any reauthorization bill that clearly delineates a certification protocol and establishes a 90-day time period after an event for determining whether or not an act of terrorism is covered by TRIA.

4. Open Issues for Further Consideration

In 2005 and again in 2007, Congress appropriately expanded the role of the private insurance market for terrorism risk and reduced the scope of the backstop provided by the federal government. Specific reform included increasing the program trigger from $5M to its current level of $100M, raising the deductibles and co-share arrangements, and establishing the federal government's entitlement to recoup any payouts that are made. Policymakers, therefore, could revisit these same areas to further expand the private market role for conventional acts of terrorism, while mindful that large-scale attacks, both conventional and NBCR, require a federal backstop.

Third party groups from across the political spectrum have suggested significant changes, from abolishing the program completely[5] to dramatically increasing the role of the private sector.[6] The following is a range of estimates based on the ongoing discussion for reforms:

[4]See Marsh report, Appendix A, page 4.
[5]Cato: "Terrorism Risk Insurance Act: Time to End the Corporate Welfare": http://www.cato.org/publications/policy-analysis/terrorism-risk-insurance-act-time-end-corporate-welfare
[6]"TRIA: To Extend or Not to Extend": http://www.insurancejournal.com/blogs/right-street/2013/09/11/304910.htm

1. Company deductible:
   - May be increased from 20% in line with growth in reinsurance industry surplus
2. Aggregate threshold:
   - Industry aggregate loss trigger may be increased from $100M to $1B or more over time
3. Company co-insurance:
   - Potentially increase insurers co-participation from 15% to 20% or more

As you grapple with these issues, it is important to keep in mind the risks associated with this transition and any expiration of the program. The ranges outlined above may cause some level of market disruption and increase the cost of insurance coverage. Mutual and regional insurers could be disproportionately impacted by these proposals. To be clear, the information above does not constitute a recommendation of Marsh & McLennan Companies and is merely intended to reflect a range of discussions on possible changes in a reauthorization of TRIA.

I applaud the Committee for scheduling this hearing to frame these issues for analysis and resolution. With the current law's expiration on December 31, 2014 quickly approaching, Marsh & McLennan Companies encourages policymakers to expeditiously reauthorize the program.

Finally, if the program is not reauthorized, there is potential for market disruption on two fronts. First, the fact that insurers' capital has increased does not mean that, in the absence of the mandatory "make available" provision, insurance carriers will offer terrorism coverage in the future. Indeed, we believe there is a meaningful risk that, if TRIA is not renewed, many property and casualty carriers will decline to underwrite this difficult to model peril.

The second area of concern is workers' compensation insurance. Terrorism exposure presents a unique challenge for workers' compensation insurance because with few exceptions, the states require coverage to be provided on an unlimited basis without the option to exclude any form of terrorism. Whether there is TRIA or not, workers' compensation carriers must pay claims without regard to fault; however, TRIA at least provides a backstop. Without a federal backstop, there is a substantial risk that workers' compensation carriers will decline to provide coverage in high-risk areas. That would potentially have a chilling impact on economic development and job creation.

Doubts about TRIA's future are already affecting the primary insurance market, particularly on the workers' compensation line of business. There are indications that carriers are negatively reacting to TRIA renewal uncertainty by non-renewing insureds with large employee accumulations in major urban cities. The market impact will likely worsen starting on January 1, 2014, as carriers withdraw coverage or issue short-term property and casualty policies.

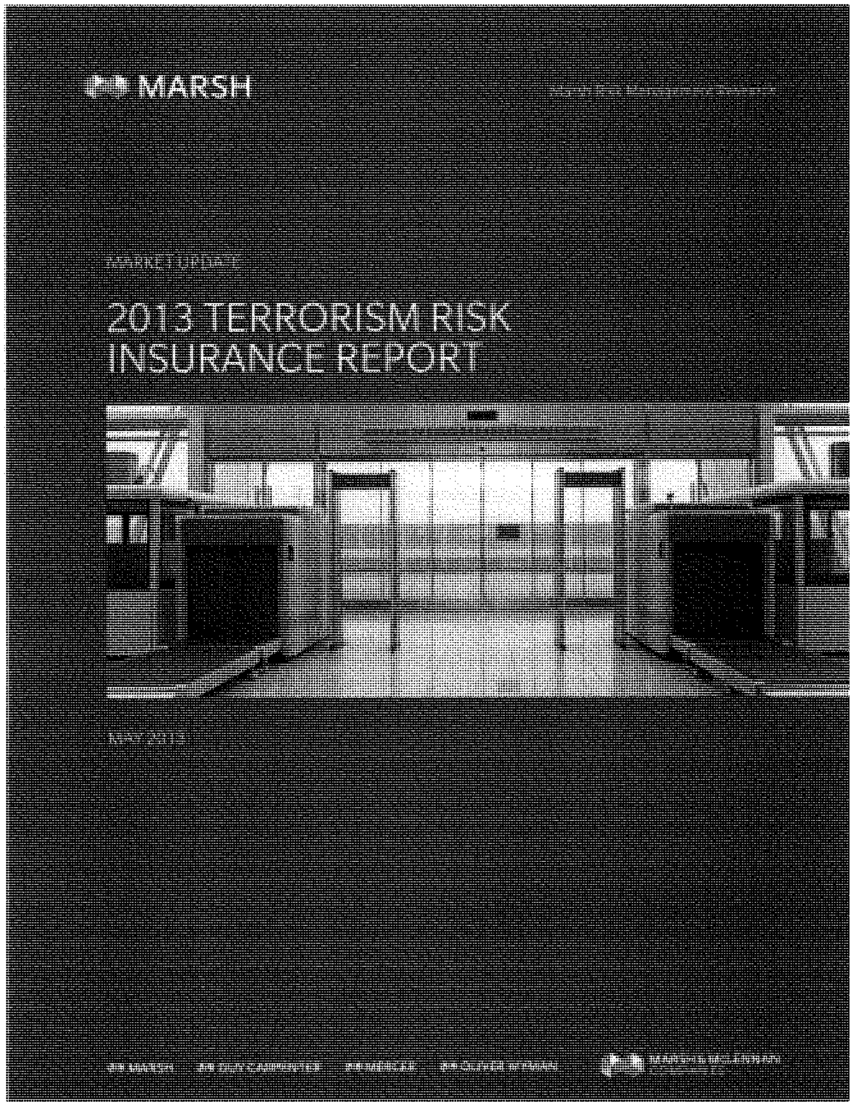
Conclusion

TRIA is the backbone of a healthy terrorism insurance market that provides policyholders with affordable and widely available coverage options. In our judgment, the existence of a growing private terrorism insurance marketplace actually serves to protect the government and taxpayers from absorbing virtually all of the financial loss in the event of a terrorist attack. As the Committee and the Senate deliberate further on the reauthorization of TRIA, Marsh & McLennan Companies is ready to collaborate with you to share our expertise and experiences on this critical public policy matter.

Appendix to Marsh & McLennan Companies Testimony

Appendix A: Marsh "2013 State of the Terrorism Insurance Market Report"
Appendix B: Evolution of TRIA

Appendix A: Marsh "2013 State of the Terrorism Insurance Market Report"


MARSH
MARKET UPDATE
2013 TERRORISM RISK INSURANCE REPORT
MAY 2013

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INTRODUCTION

The September 11, 2001, terrorist attacks created a severe market shortage for terrorism insurance. As a result, the US Congress passed legislation — the Terrorism Risk Insurance Act (TRIA) — that created a federal "backstop" for insurance claims related to terrorism events in the US as defined by TRIA. The Act became law on November 26, 2002, and has since been extended and modified twice: in December 2005 and again in December 2007, when it was renamed the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA).[1] The Act is scheduled to expire on December 31, 2014, if it is not renewed.

TRIA provides reinsurance coverage to insurers in the event of a certified terrorist act. The upcoming decision to extend TRIA as is, extend it with modifications, or allow it to expire will affect the property and casualty (P/C) insurance industry and organizations that buy terrorism insurance. As of the spring of 2013, there has been limited action in Washington, D.C., regarding TRIA's expiration, and Congress may wait until closer to the end of 2014 to determine its future.

If TRIA is not reauthorized, the number of property insurers willing to continue offering terrorism insurance is likely to decrease. According to interviews conducted by Marsh's property and terrorism experts before the 2005 extension, of 30 commercial property insurers polled, 14 (47%) confirmed they would have excluded terrorism coverage after December 31, 2005, if TRIA was not extended at that date.

With expiration less than two years away, supporters of an extension are gathering information, preparing for the possible outcomes, and asking Congress to take action. This report summarizes TRIA's history, provides benchmarking related to terrorism insurance take-up rates and pricing, and considers various scenarios regarding the future of the terrorism insurance market.

Note: Shortly before this report went to press, two bombs exploded at the Boston Marathon. As of this date, the event has not been classified as an act of terrorism under TRIPRA requirements. How and whether that event impacts the insurance markets in any way remains to be seen. But the bombing certainly raised yet again the ever-present possibility of mass violence.

1 In this report, the acronym TRIA [illegible]

EXECUTIVE SUMMARY

A key issue facing the insurance industry and insureds is the pending December 31, 2014, expiration of the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA), commonly known as TRIA. Enacted after the September 11, 2001, terrorist events, TRIA has been reauthorized twice before, both times with modifications. This report looks at the Act's history and uses Marsh benchmarking data to show trends in take-up rates, pricing, and other relevant issues.

Among the key findings:

- Congress may not fully address TRIA before the scheduled expiration at the end of 2014. If TRIA is allowed to expire or is substantially changed and the mandatory make-available provision is removed, insurers would not be obliged to offer terrorism coverage, which would affect its availability and price.
- TRIA was originally viewed as temporary and as a result, apart from the elimination in TRIPRA 2007 of the distinction between foreign and domestic acts, extensions consistently reduced government participation.
- TRIA's expiration or substantial modification at extension will almost certainly affect embedded TRIA coverage, standalone terrorism pricing/demand for capacity, and TRIA captive programs. Terrorism insurance capacity may be difficult to acquire at reasonable cost for insureds with significant exposures in a central business district of a major (Tier 1) city, or if the properties are perceived as potential targets for terrorism attacks, and/or where there have been instances of foiled plots.
- Available aggregate/terms and conditions can be restrictive in regions with past, present, or future trending terrorist activity.
- The Northeast US had the highest terrorism insurance take-up rates on average, likely due to the concentration of population centers, perceived potential for terrorist attacks, and the fact that the region was targeted in the 2001 and other attacks.
- The percentage of companies buying property terrorism insurance — the terrorism insurance take-up rate — has remained fairly constant since 2005 and has been in the low 60% range since 2009.
- Larger companies are more likely to purchase property terrorism insurance, and also to see the lowest cost as a percentage of overall property premiums.
- Among industry sectors, media companies were the most likely to purchase property terrorism insurance.
- Two likely impacts that the absence of or a serious modification of TRIA could have on the workers' compensation market are in the areas of pricing and capacity.
- Among US captive insurers managed by Marsh, 25% underwrite at least one TRIA-specific (standalone) program. Additionally, hundreds of owners use their captives to provide some element of terrorism coverage, thereby participating in TRIA.
- Global unrest has begun to affect the terror reinsurance market, not only with regard to supply and demand but in terms of how risks and coverages are defined.
- The recent bombing at the Boston Marathon had not been classified as an act of terrorism under TRIPRA requirements as of the date of this report. How and whether that event impacts the insurance markets remains to be seen. Regardless of the event being certified under TRIPRA or not, coverage for losses arising from the event will depend on clients' specific insurance contract language.

THE US TERRORISM RISK INSURANCE ACT AND ITS MODIFICATIONS

TRIA requires insurers to make terrorism insurance coverage available to their policyholders when offering to underwrite an accompanying line of business. The definition of insurer covers several categories, but the segment with the broadest reach is carriers licensed or admitted to engage in the business of providing primary or excess insurance in any state, which includes US-licensed captive insurers.

Although insurers must offer terrorism coverage, it is not mandatory for insureds to purchase the coverage, except for workers' compensation, which is defined by state statutes and compensates employees in the event of on-the-job injuries regardless of fault. Specific perils, including terrorism, cannot be declined or excluded from individual workers' compensation policies.

TRIA and its first extension required that an act be committed by an individual on behalf of any foreign person or foreign interest in order for it to be certified as an "act of terrorism" for purposes of reimbursement. This provision was removed in TRIPRA (see Figure 1). The 2007 reauthorization also provided coverage for domestic terrorism, which had previously been excluded.

CERTIFIED AND NONCERTIFIED ACTS

It is important to note that a distinction remains between acts of terrorism that are certified and those that are noncertified: Only certified acts are eligible for coverage through TRIA. An event can be certified if the Secretary of the Treasury, the Secretary of State, and the Attorney General of the United States determine the act meets all of the following criteria:

- It is considered an act of terrorism.
- It is violent or dangerous to human life, property, or infrastructure.
- It results in damage within the United States, (including US air carriers, vessels, and/or US missions, as described in the Act).
- It is committed by an individual or individuals as part of an effort to coerce the US civilian population or to influence the policy or affect the conduct of the US government by coercion.

An event cannot be certified if it does not cause property and casualty losses exceeding the $5 million threshold in the aggregate or if the act is committed as part of the course of a war declared by Congress. (Note: This shall not apply with respect to any coverage for workers' compensation).

The distinction between a certified and noncertified act of terrorism remains an important consideration for insureds and insurers alike. Although the make-available provision requires insurers to offer TRIA coverage for certified terrorism acts, some exclude coverage for noncertified acts. Therefore, businesses may wish to consider purchasing noncertified terrorism insurance, which can provide protection for those events that do not qualify as certified per the criteria listed above.

Key issues under TRIA include:

- **Trigger and threshold:** Insured losses — aggregated across all coverage lines and insurers — must exceed $5 million for an act to be considered for certification. However, there will not be any outlay of federal funds unless the event reaches the trigger of $100 million in aggregate losses.
- **Cost of coverage:** Insurers may charge an additional premium for coverage provided under TRIA, as the Act does not provide specific guidance on pricing. Although TRIA preempts state regulations for prior approval of rates, it retains a state's right to invalidate a rate as excessive, inadequate, or unfairly discriminatory.
- **Terms and conditions:** As discussed, insurers are required to make coverage available for "certified acts" to their policyholders for all subject lines of coverage. Although TRIA does not require insurers to offer specific terms and conditions, they cannot materially differ from the policy's other property and/or casualty coverages. Additionally, insurers must offer the coverage at each renewal, regardless of whether the insured previously declined.

FIGURE 1: TRIA AND ITS EXTENSIONS

TERM	NOVEMBER 26, 2002 – DECEMBER 31, 2005	JANUARY 1, 2006 – DECEMBER 31, 2007	JANUARY 1, 2008 – DECEMBER 31, 2014
Official Legislative Name	Terrorism Risk Insurance Act of 2002 (TRIA).	Terrorism Risk Insurance Extension Act of 2005 (TRIEA).	Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA).
Coverage Summary	Covered acts committed by individual(s) acting on behalf of any foreign person or interest to coerce the civilian population of the US or to influence the policy or affect the conduct of the US government by coercion.	Covered acts committed by individual(s) acting on behalf of any foreign person or interest to coerce the civilian population of the US or to influence the policy or affect the conduct of the US government by coercion.	Eliminated the distinction between acts of foreign or domestic terrorism.
Territory	US only.	US only.	US only.
Certification Threshold	$5 million	$5 million	$5 million
Federal Backstop Trigger	$5 million	$50 million in 2006, $100 million in 2007	$100 million
Insurer Retention	7% in 2003, 10% in 2004, 15% in 2005: Applied against prior-year direct earned premium.	17.5% in 2006, 20% in 2007: Applied against prior-year direct earned premium.	20%: Applied against prior-year direct subject earned premium. Subject to certain property and casualty insurance lines.
Government Share Excess of Retention	90%	90% in 2006, 85% in 2007	85%
Recoupment	Included with discretion on part of Secretary of Treasury — subject to maximum 3% per year applied to policyholders' premiums.	Included with discretion on part of Secretary of Treasury — subject to maximum 3% per year applied to policyholders' premiums.	Formula will be calculated using several factors: the size of the total loss, the amount of the industry aggregate retention as defined, the amount that the insurers actually retain, and the amount of the federal government reimbursement. There is no maximum on the amount that will be applied to future policyholders' premiums. For events that occur after 1/1/2012, the mandatory portion of any recoupment must be collected by 9/30/2017.

Source: Marsh's Property Practice

WORKERS' COMPENSATION COMPENSABILITY

The nature of a terrorist attack could have significant implications on whether injuries sustained are compensable under workers' compensation statutes. In many jurisdictions, any injuries sustained during the course and scope of employment are compensable under the statutes only if the injuries were caused by a risk specific to the employment. Simply being at work when injured is not sufficient to trigger a compensable event.

Most states focus the compensability determination on whether the employment put the employee at greater risk than that experienced by the general public. For example, with respect to acts of terrorism, employees at the World Trade Center during the terrorist attacks on September 11, 2001, were at greater risk than the general public, as those buildings were specifically targeted in the attacks. However, if the attack impacted several city blocks without targeting a specific building, then injured employees likely would not be deemed to be at a greater risk than the general public. This is essentially the same standard used to determine compensability in the event of a natural disaster such as a tornado or earthquake.

- **Adequate disclosure:** Insurers must provide policyholders with "clear and conspicuous" disclosure of both the TRIA premium being charged and the share of reinsurance provided by the federal government. If an insured rejects an offer to purchase terrorism coverage, the carrier is free to reinstate a terrorism exclusion clause (subject to state insurance regulations with standard fire policy (SFP) statutes, which in certain states do not permit the exclusion of terrorism).

- **Government participation:** The federal government will cover 85% of certified losses once insurers' deductibles have been reached. An insurer's deductible is calculated as 20% of its direct earned premium (DEP) for the prior year for the commercial P/C lines of coverage subject to TRIA.

- **Liability cap:** TRIA caps the total liability of the program and of insurers — including the insurers' participation and deductibles — at $100 billion in any one program year. If insured losses exceed $100 billion, then the allocation of loss compensation to insurers within the $100 billion cap will be determined by Congress. Insurers would not be liable for certified losses in excess of this amount unless Congress were to pass legislation increasing the limit.

- **Government recoupment:** In the event the government makes payments following a certified loss, TRIA includes provisions for both mandatory and discretionary recoupment. The insurance marketplace aggregate retention amount is the lesser of $27.5 billion and the aggregate amount, for all insurers, of insured losses from program trigger events during the program year.

TRIA AND WORKERS' COMPENSATION

TRIA's effect on workers' compensation coverage is somewhat different than it is on other lines due to the statutory nature of the coverage, which precludes the ability to limit exposure. In nearly all US states, employers are required to secure workers' compensation coverage to provide statutorily defined benefits for medical treatment and wage replacement. Exclusions and limitations to this coverage are not permitted. Because it is mandatory (via the state regulatory systems) for employers to purchase workers' compensation coverage, such coverage will always be available to employers either through private carriers, state funds, assigned risk pools, or by becoming a qualified self-insured.

After the September 11, 2001, attacks, workers' compensation insurers and reinsurers turned their focus to employee concentrations in geographic areas as a method of assessing their potential exposure to terrorist events. Computer models now allow insurers to gauge their potential exposures in a geographic area under different terrorism event scenarios, and insurers generally have adjusted their books of business accordingly in an effort to limit potential exposures.

Because TRIA provides protection for insurers, it effectively has helped a private market develop to fill in gaps in available coverage. For example, many carriers use reinsurance capacity to reduce their maximum exposure to terrorism losses and to help ensure their loss potential is within their predetermined risk tolerance.

TRIPRA's renewal, effective January 1, 2008, scaled down the protections afforded by TRIA via mechanisms such as larger deductibles and co-participations. As a result, many insurers became more vigilant in enforcing concentration guidelines. Uncertainty around TRIA's potential expiration or extension in 2014 has led some insurers to not renew certain programs for organizations with large employee concentrations in major cities. This trend could continue as TRIA's 2014 deadline draws closer.

TRIA AND CAPTIVE INSURERS

Guidance issued by the Department of Treasury affirmed that TRIA applies to captive insurers and risk retention groups that meet the definition of a qualified insurer, as set forth in Section 102 of the Act, "Definition of Insurer." Essentially, any entity that falls within the state licensed or admitted category and receives and reports direct earned premium is considered to be an insurer under TRIA. Captives are included to the extent they provide direct coverage only, and must be domiciled in the US to be eligible for inclusion under TRIA. (All references to "captives" in this report apply to US-domiciled captives only.)

To the extent the coverage is offered as part of an existing policy — embedded in the property program, for example — the terrorism coverage must not materially differ in the terms and conditions offered. This does not, however, prohibit an insured from seeking TRIA-specific coverage in a separate transaction. Captives also must comply with TRIA's disclosure requirements. The National Association of Insurance Commissioners (NAIC) has reporting forms that were approved by the Department of Treasury. The forms are available at http://www.naic.org/cipr_topics/topic_tria.htm

Using a captive to insure an organization against acts of terrorism can be a viable, cost-efficient alternative or adjunct to a traditional insurance program. There are many considerations that organizations should take into account when determining whether to use their captive to provide or supplement their terrorism insurance.

POTENTIAL ADVANTAGES OF ACCESSING TRIA THROUGH A CAPTIVE

- **Profit:** If there are no losses, the actual expense of the terrorism insurance program to the consolidated group is limited to the cost to operate the captive, which is generally only a fraction of the premium paid.

- **Relative ease:** It is relatively easy to add terrorism coverage to an existing captive. Doing so typically requires demonstrating a business need and sound plan of operation to the captive insurance regulator, which will often promptly approve the addition or expansion of a terrorism insurance program.

- **Enhanced coverage:** Generally, captives are willing and able to provide terrorism insurance coverage using a customized policy form, which may result in coverage that is better aligned to needs, including covering perils generally excluded or limited by traditional insurers. An example of this is captive insurers providing coverage for nuclear, biological, chemical, and radiological (NBCR) perils. Although TRIA guidance states that the Act provides reinsurance protection to insurers when they offer NBCR (and a loss occurs), TRIA does not require insurers to offer the coverage. Given the lack of a TRIA mandate, combined with the perceived risk, NBCR is not widely available in the traditional insurance marketplace. Captive insurers are able to offer this coverage and gain access to reinsurance afforded through TRIA. It is also possible to cover other perils in a similar fashion, as is occurring in some cases based on the unique needs and coverage limitations experienced by those seeking a viable risk transfer alternative.

TERRORISM INSURANCE MARKET

Terrorism insurance take-up rates generally have remained steady over the past few years. Most companies that purchased terrorism insurance in the past still do so as insurers continue to underwrite the risk, with the support of the TRIA backstop. The reauthorization of TRIA through 2014 has afforded needed capacity in the market for terrorism insurance.

Property insurers are able to include terrorism insurance in their risk portfolios at typically nominal rates to insureds. Clearly, the demand for terrorism risk insurance remains and the existence of TRIA plays a major part in the availability and affordability of the coverage.

TERRORISM INSURANCE TAKE-UP RATES BY YEAR

The percentage of companies buying property terrorism insurance — the terrorism insurance take-up rate — has remained fairly constant since 2005. In 2003, the first full year TRIA was in effect, the take-up rate was 27% but has since increased steadily, remaining in the low 60% range since 2009 (see Figure 2).

TAKE-UP RATES BY COMPANY SIZE

Looking at take-up rates by company size (see Figure 3), it is useful to consider four categories of total insured value (TIV):

- Companies with TIV in excess of $1 billion typically work with several insurers and likely pay large premiums. Of those companies that use their existing captives or establish new ones to provide TRIA, the majority are in this TIV group.

- Companies with TIV between $500 million and $1 billion are large organizations that also typically work with multiple insurers and have layered programs.

- Companies with TIV between $100 million and $500 million tend to have no more than three insurers involved in their insurance programs.

- Companies with TIV less than $100 million generally entail a smaller spread of risk, have lower overall premiums, and often work with a single insurer.

Changes in take-up rates by company size were marginal from 2010 to 2012. Companies with TIV less than $100 million had the lowest take-up rates among those analyzed, with 59% purchasing property terrorism insurance in 2012.

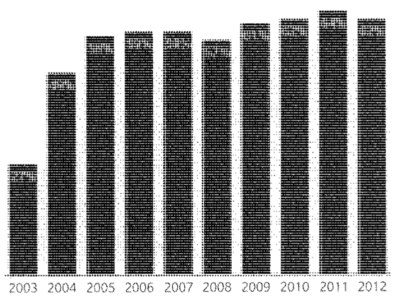
Conversely, the take-up rate for companies with TIV higher than $100 million was nearly 66% in 2012. This may be due to a perception that larger companies are more susceptible to an attack or because smaller companies typically have lower insurance budgets with which to purchase insurance.

TAKE-UP RATES BY INDUSTRY

Media clients purchased property terrorism insurance at a higher rate — 81% — than did those in any other industry segment in 2012.

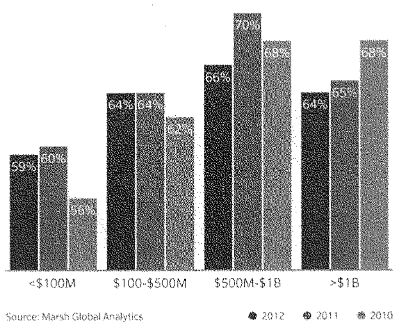
Companies in the health care, financial institutions, education, and public entity sectors had the next highest take-up rates among the 17 industry segments surveyed, all above 70%. This may be due in part to concentrations in those sectors of organizations in central business districts and in major metropolitan areas, which are likely perceived as being at a higher risk for terrorism. The manufacturing, energy, and chemicals sectors were the only three in which take-up rates did not exceed 50% in 2012 (see Figure 4).

FIGURE 2: TERRORISM INSURANCE TAKE-UP RATES BY YEAR



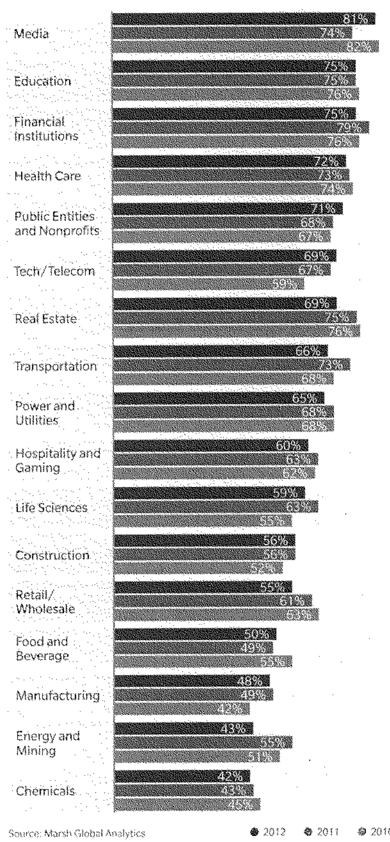
Source: Marsh Global Analytics

FIGURE 3: TERRORISM INSURANCE TAKE-UP RATES BY TIV



Source: Marsh Global Analytics

FIGURE 4: TERRORISM INSURANCE TAKE-UP RATES BY INDUSTRY

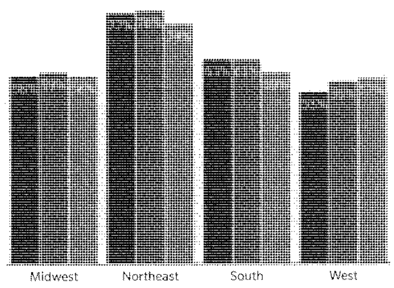


Source: Marsh Global Analytics

TAKE-UP RATES BY REGION

A higher percentage of companies in the Northeast — 77% — purchased property terrorism insurance than in any other region. This is likely attributed to the Northeast's concentration of large metro areas, including Washington, D.C., and New York City; the perception that major cities may be at a higher risk of a terrorist attack; population density; and the fact that the 2001 attacks targeted sites in the region. The West saw the lowest take-up rate, at 53% in 2012 (see Figure 5).

FIGURE 5: TERRORISM INSURANCE TAKE-UP RATES BY REGION



Source: Marsh Global Analytics

TYPES OF TERRORISM COVERAGE PURCHASED

Approximately 95% of clients that purchased terrorism insurance did so as part of their property policies rather than as standalone placements. However, standalone policies are an important alternative and/or supplement to TRIA coverage for some companies. The primary industry segments purchasing standalone policies have been hospitality, large real estate firms, and financial institutions. Lesser but still significant amounts were purchased in the retail, media, transportation, public entity, and utilities segments.

Before the 2007 extension, companies that purchased terrorism coverage as part of their property policies generally purchased both TRIA coverage and noncertified acts coverage. However, because TRIPRA expanded the definition of covered acts to include domestic terrorist events, many companies since have elected not to purchase noncertified terrorism insurance in addition to purchasing TRIA coverage as part of their property policies. Nevertheless, certain events may still be considered noncertified, although to a more limited extent than before TRIPRA, which removed the foreign terrorism requirement to trigger certification.

More companies now are securing terrorism insurance through their captives and are purchasing reinsurance to cover their retention or liability under TRIA. Typically, those captives that do purchase reinsurance often buy coverage for noncertified terrorism exposures in addition to TRIA coverage.

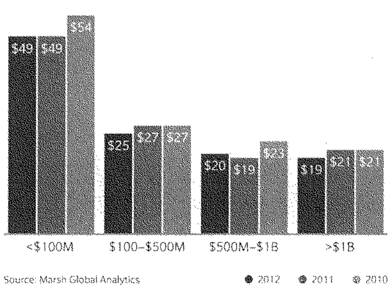
THE COST OF TERRORISM INSURANCE

It is useful to measure the cost of terrorism insurance both as a premium rate — premium divided by TIV — and as a percentage of a company's overall property premium. Analyzing costs by premium rate allows companies to track what they paid in absolute terms; evaluating the cost as a percentage of their total premium shows how terrorism coverage affected their overall property insurance budget.

COST BY COMPANY SIZE

Property terrorism insurance rates typically decrease as the size of the company increases (see Figure 6). Since 2010, companies with TIV less than $100 million experienced moderate median rate decreases, from $54 per million in 2010 to $49 per million in 2012; however, their terrorism premium rates remained significantly higher than those of larger companies. Median rates for the largest companies stood at $19 per million in 2012. This generally is in keeping with overall insurance pricing patterns: Larger companies typically purchase more insurance, which leads to lower rates compared to rates for smaller companies.

FIGURE 6: TERRORISM INSURANCE PRICING – MEDIAN RATES BY TIV (RATES PER $MILLION)

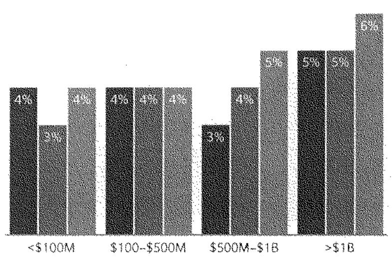


Source: Marsh Global Analytics

The cost as a percentage of overall property premiums (see Figure 7) was similar for all companies, regardless of TIV. Modest changes — no more than one percentage point per year — were seen across the board, although companies with TIV between $100 million and $500 million remained flat at 4% over the past three years. Only companies with TIV less than $100 million experienced an increase from 2011 to 2012, and only companies with a TIV range between $500 million and $1 billion saw a decrease.

Although this suggests that the cost of terrorism coverage generally remained the same in the various size classes, individual businesses may have experienced significant swings based on their property insurance program's performance. For example, organizations with significant catastrophe (CAT) losses may have faced large increases in their overall property insurance program, but little change in their terrorism insurance pricing, resulting in a smaller percentage of their overall premium being attributed to terrorism coverage. Conversely, companies that had favorable loss histories in recent years may have experienced rate decreases in their overall programs while their terrorism insurance pricing remained constant or decreased, which may show in the analysis as an increase in terrorism pricing as a percentage, despite no overall increase in total costs.

FIGURE 7: TERRORISM INSURANCE PRICING AS PERCENTAGE OF PROPERTY PREMIUM BY TIV



Source: Marsh Global Analytics

FIGURE 8: TERRORISM PRICING – MEDIAN RATES BY INDUSTRY (RATE PER MILLION)

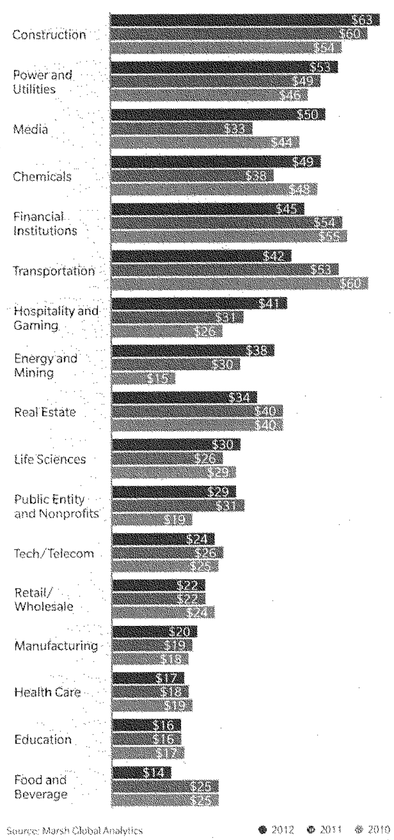
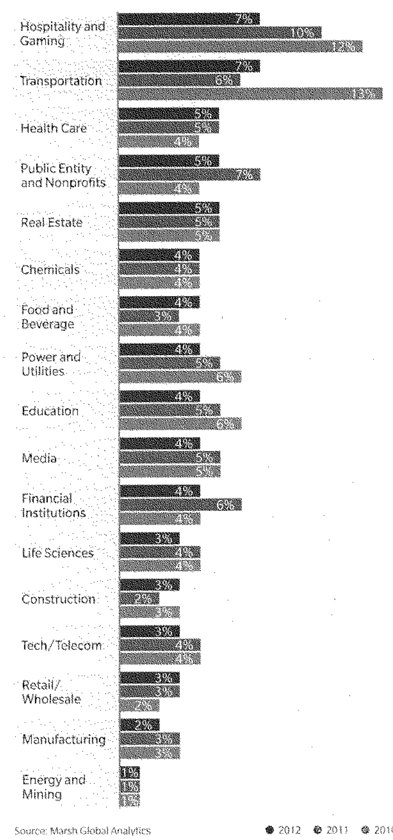


FIGURE 9: TERRORISM INSURANCE PRICING AS A PERCENTAGE OF PROPERTY PREMIUM BY INDUSTRY



COST BY INDUSTRY

Compared to rates in 2011, median property terrorism insurance premium rates decreased in 2012 for seven of 17 industry categories: financial institutions, transportation, real estate, public entity and nonprofit, technology/telecom, health care, and food and beverage. Organizations in the financial institutions, food and beverage, and transportation sectors experienced the most significant decreases.

Rates increased most significantly for media companies, while construction, power and utilities, chemicals, hospitality, energy, life sciences, and manufacturing companies also experienced increases in their median rates (see Figure 8). Although each company's policy is priced based on its unique exposures, it is possible that a combination of prior CAT losses and location — namely businesses located in a central business district — may have contributed to any increases.

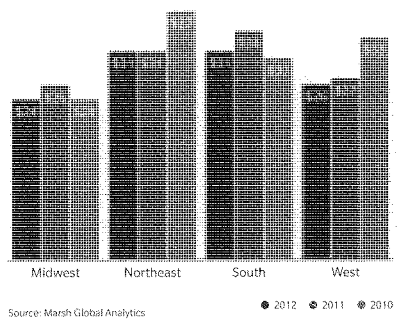
Overall, construction companies paid the most for their terrorism insurance, at a median rate of $63 per million, up from $54 per million in 2010. Companies in the food and beverage, health care, and education sectors paid the least for coverage, with median rates less than $20 per million. Food and beverage firms experienced the most significant reductions in median rates over the past three years.

When analyzing terrorism insurance pricing as a percentage of overall property premiums, hospitality and transportation companies paid the largest share, allocating 7% of their total property programs, which also represents the largest increase as a percentage of total property insurance cost among all industry groups (see Figure 9). No other industry sector paid more than 5% of its total property premium for terrorism coverage. Energy companies continued to pay the lowest, allocating only 1% of total property premiums to terrorism insurance over the last three years.

COST BY REGION

Companies in the Midwest paid the lowest rates for property terrorism insurance in 2012, followed closely by companies in the West (see Figure 10). Based on median premium rates, terrorism insurance was the most expensive in the South and in the Northeast, although the regional variation has narrowed. Companies in the Northeast experienced the highest median rates per million.

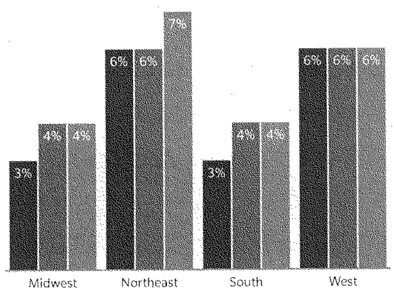
FIGURE 10: TERRORISM INSURANCE PRICING – MEDIAN RATES BY REGION (RATES PER MILLION)



Source: Marsh Global Analytics

Terrorism insurance pricing as a percentage of property premium varies slightly in the four US regions analyzed (see Figure 11), accounting for an average of 3% of total property premiums for companies in the Midwest and South, and 6% in the West and Northeast. Much of this difference can be explained by regional differences in terrorism exposure. Companies in major metropolitan areas — for example, New York, Washington, D.C., and Boston — are likely to pay a higher premium for their terrorism coverage, which results in a larger percentage of their overall property insurance costs being dedicated to terrorism coverage.

FIGURE 11: TERRORISM INSURANCE PRICING AS PERCENTAGE OF PROPERTY PREMIUM BY REGION



Source: Marsh Global Analytics

US property terrorism insurance rates generally have decreased or remained flat over the past three years. However, the overall property insurance marketplace was affected in 2011 and 2012 by a number of significant CAT events in the US and globally, contributing to slight increases in property and terrorism insurance rates. Additionally, the release of updated CAT models from modeling firms AIR Worldwide and RMS contributed to a general push by insurers to increase rates or to slow or cease rate decreases. Companies without significant CAT exposures or with favorable loss histories were less likely to experience rate increases.

CONSIDERATIONS IN USING CAPTIVES FOR TERRORISM COVERAGE

Among US captive insurers managed by Marsh, 25% underwrite at least one TRIA-specific (standalone) program. Additionally, hundreds of owners use their captives to provide some element of terrorism coverage, thereby participating in TRIA. Captive insurers' participation stems both from TRIA's make-available provision and from the standalone programs they underwrite. It is common for the policyholder to accept the captive's offer of terrorism insurance when the captive is also providing property or casualty insurance.

In more complex scenarios, captives provide standalone terrorism programs, often as a supplement to a traditional insurance placement. These arrangements most commonly involve providing insurance for property losses resulting from terrorism, not standalone liability placements. In some cases, the captive is asked to provide limits in excess of what is available in the commercial market and/or to provide additional breadth of coverage.

An example of a more complex structure is a captive providing $500 million in excess of $500 million of conventional terrorism insurance purchased from commercial insurers, $1 billion of NBCR coverage, and wraparound protection for the commercial insurance program. The wraparound element provides for payment of losses by the captive insurer if the commercial insurance program does not result in the expected coverage after a loss.

CAREFUL EVALUATION REQUIRED

Although implementing a terrorism insurance program within an existing captive (or forming a new captive to implement a terrorism insurance program) is relatively straightforward, it is important to thoughtfully evaluate the feasibility and appropriateness of doing so prior to implementation and again during subsequent renewals. Several key considerations follow.

- Captives are included in the definition of insurers under TRIA according to Department of Treasury guidance; however, captive owners have been specifically cautioned against "gaming" the program.

These cautions are in recognition of the inherent conflict of interest and unusual level of control a policyholder (typically the captive's parent and other affiliated companies) has over an insurer in a captive insurance transaction. The cautions emphasize that captive owners should not take actions that would improperly reduce an organization's overall share of a loss — for example, captive insurers should not deliberately price the premium low in order to reduce the captive's TRIA deductible.

- Capitalization must be determined and provided. Two major factors are considered when determining capitalization. The primary consideration is that capitalization must be sufficient to satisfy the responsible domicile's insurance regulator. Captive insurance company regulators apply different standards, but are primarily concerned with statutory minimums and ensuring that the captive insurer has the capacity to meet its reasonably foreseeable obligations to policyholders. Regulators also consider such traditional factors as reinsurance protection in this analysis, as well as nontraditional "assets" such as letters of credit posted with the regulator. Second, capitalization should be evaluated based on appropriateness considering the overall business plan and objectives of the captive.

- Premiums charged by the captive should be based on current market prices. If premiums are not thoughtfully derived and supported, financial penalties, including not recovering in the event of a loss, may apply.

- Captives, like all subject insurers, may be required to submit information on terrorism premium rates for review by NAIC and the Secretary of the Treasury. Should actual aggregate insured losses exceed $100 billion — the amount at which the federal government's annual liability is capped — it could result in a policyholder receiving less than the stated policy limits.

- TRIA permits insurers to obtain reinsurance coverage for all or any portion of any loss not covered by the Act. No payments will be made for acts of terrorism resulting in aggregate insured losses of less than $100 million. The effect of the trigger is to introduce uncertainty in the event of smaller losses. A worst-case scenario could see an insurer exposed to up to 100% of a loss of up to $99,999,999.

- Timing must be considered when creating a captive or amending its purpose to write new lines of coverage in order to avail itself of coverage provided by TRIA. It typically takes between 30 and 60 days to establish a new captive. With an existing captive, the timeframe will depend on its current scope and desired amendments, but it is likely to take at least seven days to secure the required approvals and incept the coverage.

- The startup and ongoing administrative costs of a US-domiciled captive should be considered and can vary depending on several factors, such as scope and fees for management, audits, legal advice, and actuarial work required.

- Under TRIA, insurers — including captives — are required to process claims in accordance with customary business practices. Other procedures may also be prescribed by the Secretary of the Treasury.

- If a captive insurer is affiliated with other organizations that qualify as insurers under TRIA, the direct earned premiums of the affiliated insurers will be considered along with the captive's when determining insurer deductibles.

STANDALONE PROPERTY TERRORISM INSURANCE MARKET

FIGURE 12: TERRORISM INSURANCE MARKET CAPACITY (IN $MILLIONS)

INSURER/REINSURER	CAPACITY
Chartis	$1,500
Berkshire Hathaway	$1,000
Lloyd's	$900
Lancashire Insurance Group	$200
AXIS Specialty	$150
Hiscox USA	$100
Validus	$100
Western Re	$85
ACE Global Markets	$50
Montpelier Re	$50
Transatlantic Re	$50
Beazley US	$50
Torus	$40
IRI/Westport	$40
Aspen Re	$30
Inter Hannover	$25

Note: The theoretical marketwide capacity would be difficult to acquire at a reasonable cost for any individual client, and few clients seek coverage above $1.5 billion. For a client with significant exposures in central business districts of Tier 1 cities or those with exposure schedules with properties perceived as targets for terrorism attacks or where there have been instances of foiled plots, the available capacity is lower. Insurer capacity (and pricing) is also affected by accumulation of aggregates within ZIP codes including Tier 1 cities such as New York, Chicago, Washington, D.C., and San Francisco.

Source: Marsh's Property Specialized Risk Group. Data as of April 23, 2013.

Terrorism and political violence events remain a threat worldwide. Demand for terrorism and political violence insurance coverage has grown in the Middle East, Asia, and North Africa following the so-called Arab Spring of 2010.

Standalone capacity can vary considerably, primarily due to:

- **Location of risk:** The demand for coverage in major metropolitan areas has a substantial affect on the available capacity.
- **Insurer's accumulation of exposure:** Most insurers place aggregate limits on the risks they will take, which can limit capacity in certain locations.
- **Concentration of exposure:** Terrorists attack targets of opportunity. Although it is certainly possible that an attack could occur in a rural area, a remote town, or a small city, demand for coverage will likely be higher in major metropolitan areas due to the concentration of exposures and higher perception of risk.

MARKET CAPACITY

- Standalone capacity has increased significantly for exposures outside central business districts.
- Approximately $750 million to $2 billion per risk in standalone capacity is available to companies that do not have sizeable exposures in locations where standalone insurers have reached or are approaching aggregation limits. Capacity in excess of $2 billion is available but is more expensive.
- For locations where standalone insurers have aggregation issues, the estimated market capacity is approximately $850 million or lower in some cases. Additional capacity can be accessed, but typically at significantly higher rates.
- Monitoring of aggregates is a priority for insurers, with capacity in top-tier cities being priced accordingly.

TERRORISM REINSURANCE MARKET

Global unrest has begun to affect the terror reinsurance market, not only with regard to supply and demand but in terms of how risks and coverages are defined. Although there is an abundance of capacity in the market due to the absence of a major recent terrorism insured loss (resulting in a stable to softening treaty terrorism market), civil unrest and/or riot coverages in some international terrorism programs are impacting several carriers. Indeed, the dramatic increase in global unrest has caused an increased frequency of localized or territory-specific losses in the facultative reinsurance market. As noted earlier, the Boston Marathon bombing's impact on the insurance markets is still to be determined as of this writing.

On a per-risk basis, there is an estimated $2.5 billion of capacity, approximately, for terrorism and sabotage coverage available in the facultative reinsurance market at the time of this writing. Capacity for the broader political violence coverage varies depending on world events and losses within specific territories. As loss activity increases and pricing subsequently rises, capacity is attracted to the territory. Nevertheless, the recent increase in loss frequency in the facultative market has not yet affected the general market and a general market hardening is not presently anticipated. Instead, there have been changes to capacity and pricing at the local level.

GLOBAL UNREST

The scale and damage caused by the recent global unrest has prompted a number of insureds in several countries and regions to broaden the coverage they purchase in an effort to mitigate any potential gaps. Coverage trends, however, vary by country and region. Rather than take a one-size-fits-all approach, reinsurers are increasingly evaluating coverage needs on a per-territory or per-region basis.

The unrest occurring in the Middle East and North Africa has led to a change in coverage purchasing behavior. As the nature of events in the region continues to change, a number of reinsurers are reassessing their overall protection. While strikes, riots, and civil commotions are typically included in an "all risk" policy, larger scale political upheavals — including events categorized as insurrection, civil strife, rebellion, revolution coup d'état, mutiny, and war — are covered only by the specialist political violence market.

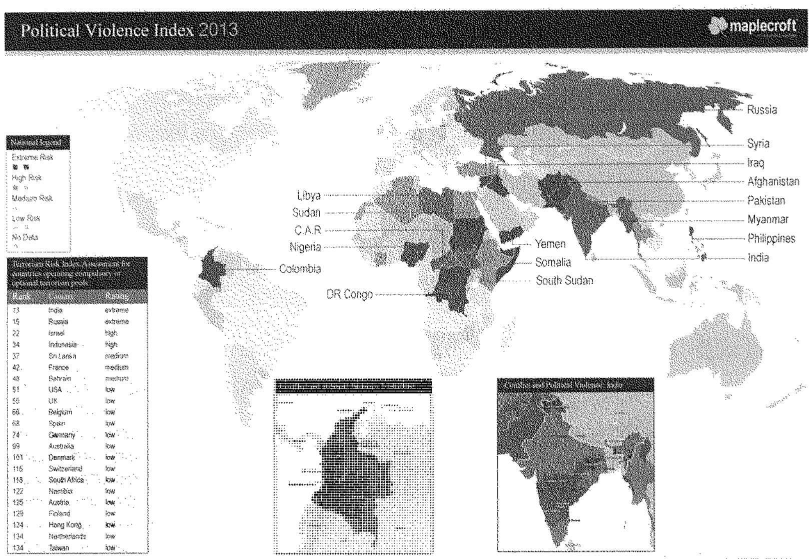
The volatility in the region has therefore led to increased demand for political violence coverage, as carriers are looking for comprehensive reinsurance coverage to ensure that claims will be dealt with effectively and swiftly. Recent events in countries such as Tunisia and Egypt have illustrated how situations can rapidly escalate from those categorized by reinsurers as strikes, riots, and civil commotion to full political violence events. By purchasing full political violence coverage, reinsurers and insurers have a broad spectrum of insurance, meaning protection is provided regardless of how the event is defined. As a result, the market has become more restrictive in some Middle Eastern and North African countries.

Loss history and incorrect interpretations of terrorism coverage in the past have also emphasized the importance of understanding the subtle differences in coverage. In Israel, for example, attacks by Hezbollah were classed as war losses by the government rather than as terrorism losses.

INTERNATIONAL SCHEMES — GOVERNMENT POOLS AND TRIA

To help insureds manage the global terrorist threat (see Figure 13), terrorism reinsurance pools have been created in a number of countries. The pools were established in reaction to the specific threats faced within each country, and each pool generally requires a declaration by the national government that a terrorist event has occurred to trigger coverage. In the countries where compulsory or optional terrorism reinsurance pools exist, property insurance policies can be extended to include terrorism coverage in accordance with the local pool. In such situations, the application of the standalone terrorism, sabotage, and/or political violence policy should be either difference in conditions (DIC), difference in conditions and limits (DIC/DIL), or primary of the locally issued property policy pool coverage depending on the pool being accessed.

FIGURE 13: GLOBAL POLITICAL VIOLENCE RATINGS



Maplecroft's *Political Violence Index 2013* illustrates global political violence and terrorism risks. The accompanying table summarizes the compulsory and optional terrorism pools that operate around the globe. Note: The table includes Northern Ireland in the rating of the United Kingdom; however, Northern Ireland maintains its own terrorism pool, "Criminal Damage Compensation Scheme Northern Ireland."

Source: Maplecroft

FUTURE OF TRIA/TERRORISM INSURANCE IN THE UNITED STATES

Since TRIA's enactment in 2002, terrorism insurance has been widely available for property and other qualifying lines of insurance. Insurers are mandated to offer TRIA as part of their original quote, and the coverage must substantially follow the terms and conditions of the policy to which the TRIA cover attaches.

POTENTIAL RAMIFICATIONS IF TRIA EXPIRES OR IS MATERIALLY CHANGED

If TRIA is allowed to expire or is substantially changed and the mandatory make-available provision is removed, insurers would not be obliged to offer terrorism coverage. The pricing that insurers charge for TRIA is effectively subsidized, in part because the federal backstop does not charge insurers for the protection it offers. Therefore, the TRIA premium charged by insurers without TRIA in place is likely to be considerably higher.

Potentially, property reinsurance capacity and competition could positively influence the supply of terrorism capacity; however, available coverage and limits would not be as readily available. In particular, this may impact companies that have substantial property exposures in central business districts and where reinsurance capacity would be diminished and insufficient to meet insurers' demands.

Additionally, some industries are susceptible to certain insurance requirements, such as mortgage lender requirements with real estate companies. Within TRIA's current structure, the limits available for terrorism insurance are typically sufficient for real estate companies to meet their risk transfer and lender requirement needs. A change in the Act's structure could potentially cause a gap in demand and availability. This susceptibility is not limited to "central business districts" or major cities.

STANDALONE MARKET

The main alternative for a property terrorism risk transfer mechanism if TRIA is not reauthorized would be the standalone terrorism insurance market. As standalone capacity is finite, the cost of this capacity likely would be considerably higher in areas or cities where demand is high, such as major metropolitan areas, central business districts, iconic buildings, ports/airports, and even "soft targets" such as shopping malls. This market dynamic varies considerably by location. In certain high-risk cities — such as New York or Washington, D.C. — the cost of standalone terrorism insurance capacity can be five to 10 times higher than the current pricing for TRIA embedded as part of property programs. However, standalone capacity in certain ZIP codes is so limited that approximately 10% of the current embedded TRIA limit may be currently available in the standalone property terrorism market; should TRIA no longer be in effect, capacity will be affected. In areas perceived to be lower risk, the costs and capacity can be similar between the standalone property terrorism market and TRIA embedded as part of an "all risk" property program.

STATE REGULATIONS

It is important to note that state insurance regulations in 14 of 29 states where standard fire policies (SFP) are mandated do not permit property terrorism exclusions or sublimits for fire caused by a terrorism event. In the absence of substantial market reinsurance capacity to offer insurers an alternative reinsurance mechanism to TRIA, this would likely impact the level of fire or "all risk" property capacity these insurers could offer in areas or cities where they are concerned about the aggregation of terrorism risk. For companies with locations in those areas or cities, this will result in less available fire/"all risk" property insurance, as well as terrorism coverage if TRIA is materially changed or not reauthorized.

In the absence of TRIA, companies with single-carrier property insurance programs and large limits ($100 million or more) in high-risk areas or those in states that have "fire following/no terrorism exclusion permitted" may require insurance programs to be shared and layered in order to achieve desired limits. This will increase the number of insurers needed to provide the same level of insurance and likely will increase the total cost to insureds.

PROPERTY PROGRAMS

Without a reauthorization of TRIA, shared and layered property insurance programs likely will be subject to substantial differences by layers of insurance on the extent and terms of terrorism coverage. The main implications of such potential differences are using higher-cost standalone terrorism capacity to fill gaps in insurance programs, increased risk if self-insuring gaps, and non-concurrent coverage in the event of a loss.

WORKERS' COMPENSATION

In addition to property insurance, other coverage lines likely will be impacted if TRIA expires or is significantly changed, particularly workers' compensation insurance, as workers' compensation insurers are not permitted to exclude terrorism from their policies. Insurers are concerned about potential aggregation of risk, which may impact the availability of workers' compensation insurance should TRIA materially change or expire. Where these insurers are also offering other lines of insurance, such as property, the combined aggregate exposure likely will further limit their ability or willingness to offer substantial property limits.

The workers' compensation market has been affected by the risk of a terrorist attack, even with the reinsurance backing TRIA provides. Because TRIPRA scaled down the protections afforded by the original 2002 Act (via mechanisms such as increased retentions), it forced insurers to be more vigilant in enforcing concentration guidelines. For example, some carriers have not renewed marquee financial services accounts because of the concentration risk in cities perceived to be terror targets.

If TRIA is either modified significantly or not renewed in 2014, the expectation is that employers will continue to have sufficient insurers from which to purchase workers' compensation coverage in order to comply with state laws. Since such coverage is statutory and cannot be limited, the terms of workers' compensation coverage will not be impacted by the absence of TRIA. An exception to this is the market for excess coverage for self-insured employers. Immediately after the September 11, 2001, attacks, some excess insurers responded by capping their liability at levels less than full statutory coverage. However, in the past, other insurers responded by writing statutory coverage above the limits of the underlying carriers; competition for workers' compensation business continues to exist in the market in 2013, albeit at higher prices.

Two likely impacts that the absence of or a serious modification of TRIA could have on the workers' compensation market are in the areas of pricing and capacity. It is expected that the reinsurance market would likely increase pricing because of the increased potential exposure. This would, in turn, have a trickle-down effect on the primary workers' compensation marketplace. Further, the ability of insurers to use reinsurance capacity to manage their maximum tolerable losses could prove more difficult, especially for the terrorism perils of NBCR events. This could significantly alter carriers' risk appetites and their willingness to offer coverage to employers with large employee accumulations.

In addition, insurers have had more than 10 years to collect premium and build surplus for the potential exposure to terrorist acts. Because of this, there arguably is capacity in the workers' compensation industry to respond to a terrorist event should one occur. One question that arises: Is that accumulated capacity adequate in the event TRIA is allowed to sunset?

While not frequently mentioned, the employers' liability component to the workers' compensation policy may also be a factor. When barred by workers' compensation's exclusive remedy from suing the employer, claimants will frequently sue others — for example, fire suppression system installers or security guards — in an effort to find a deep pocket. The employer is then brought in via third-party practice, and the employers' liability policy would have to respond. To a lesser extent, serious injuries and allegations of wanton conduct by the employer tend to produce attempts to surmount the workers' compensation bar in search of higher tort damages. For example, there could be allegations that cost-cutting measures resulted in a reduction of the number of security guards, despite an awareness of a serious threat.

GENERAL LIABILITY

Unlike property insurance, the general liability (GL) insurance market does not have robust standalone terrorism capacity. While it is possible to model the potential of loss with a single building of "$X" value, insurers typically find it difficult to become comfortable with GL risks, because the frequency, severity, and instrumentality of loss or number of victims cannot be predicted. Additionally, in the absence of TRIA, although there is no terrorism exclusion in a typical GL policy, other exclusions and conditions could be brought to bear by an insurer seeking to avoid exposure to large terror losses. For example, depending upon the circumstances, one might see the following types of defenses: late notice, pollution exclusion, professional liability, or war.

CAPTIVES

Organizations that employ captives also are likely to be affected in the event TRIA is allowed to expire or is significantly changed. Captives are widely used to supplement what is available in the commercial market, and, in some cases captive insurers are the only available option for certain layers and/or perils. This is most common in areas of higher perceived risk such as for property or employee-related coverages in major cities. Generally speaking, since captives are best suited to primary operating layers, or as a mechanism for accessing risk transfer solutions, it is very likely that, absent TRIA, captive utilization for terrorism coverage would change significantly. Without TRIA, captives will likely revert to their traditional role of providing commercial reinsurance access to the captive sponsor (where such reinsurance exists) or simply as a mechanism for funding lower-level retentions more consistent with the net retentions that are in effect under TRIA.

CYBER RISK

Although there has been no precedent where TRIA has been applied in response to a cyber attack, a cyber-terrorist attack arguably could trigger coverage under TRIA so long as the Treasury Secretary certified the attack as an "act of terrorism" and all other statutory requirements were met. Thus, TRIA could be instrumental in providing stability in the event of a "cyber Pearl Harbor," in which catastrophic damages resulted. Notably, as the severity and frequency of cyber attacks have grown more prominent, several proposals have been made to clarify that TRIA could apply as reinsurance in the event of a massive cyber attack. Were that clarification realized, TRIA could spur additional capacity in the cyber market.

IMPLICATIONS FOR THE REINSURANCE MARKET

If TRIA is not extended or is substantially modified, the impact on embedded terrorism insurance coverage, standalone terrorism pricing/demand for capacity, and TRIPRA captive placements are likely to impact the reinsurance marketplace as well. Although the standalone terrorism market continues to remain an alternative to TRIA coverage offered as part of property "all risk" policies, there is not sufficient capacity for regions with the highest demand for insurance to meet the needs of all policyholders. Coupled with limited availability of standalone reinsurance capacity and continued perceived limitations on the reliability of terrorism risk models, the insurance markets are not well positioned to be a viable alternative replacement to TRIA or other government-mandated and -supported terrorism risk transfer mechanisms in the United States.

Terrorism catastrophe exposure continues to be of particular interest to property and workers' compensation insurers and to rating agencies for several reasons. First, unlike property insurers, in most cases workers' compensation carriers are obligated to cover terrorism for every risk in their portfolios. Second, unlike for natural perils, A.M. Best requires a carrier to model the severity of its highest potential attack scenarios as well as a percentage of policyholders' surplus. This could result in some notably high results with the potential of being stress tested, and, in select cases, could impact an insurer's rating.

MERITS OF REINSURANCE PROTECTION

Although the need for TRIA is clear, reinsurance protection can help companies withstand the nonrenewal or alteration of the program. Indeed, even though the federal backstop currently is in place, many insurers seek to ensure additional protection via reinsurance. These standalone reinsurance protections typically exclude losses resulting from NBCR instruments, but would protect all losses from the property, casualty, and workers' compensation policies they underwrite. Standalone reinsurance pricing continues to vary depending on the geographical location of the risk(s) and proximity of the risk to a perceived target of terrorism.

Carriers that are perceived to benefit from lower TRIA deductibles (based on direct earned premiums) likely will see a greater impact and may need to reduce their aggregate exposure to terrorism on the front end (reduce writings) or buy more reinsurance protection. While there currently appears to be ample capacity for insurers that buy standalone terrorism reinsurance, increased demand would likely result in constrained capacity and higher prices. The potential scenario that an insurer suffers a loss less than the current $100 million (and potentially higher future) industry trigger — without any reimbursement from TRIA — is gaining heightened attention by carriers and the rating agencies.

Higher reinsurance limits and costs could make it less affordable for smaller companies to buy sufficient coverage. Any dramatic change in TRIA potentially could lead to contraction in the marketplace in both insurance and reinsurance. In a recent briefing, A.M. Best indicated that material changes in TRIA would raise rating concerns especially in cases where:

- Net exposure to terrorism (excluding the benefits of TRIA) exceeded 20% of capital and surplus.
- Aggregate exposures of risks in certain geographic areas are notably high.
- The locations of exposures within these areas potentially impact capitalization.

In its discussions with insurers, A.M. Best is questioning potential plans to track exposure, underwrite aggregates more conservatively, not renew specific risks, and/or increase/change reinsurance purchases should their net TRIPRA retention notably increase. Overreliance on the federal backstop is not considered to be a good substitute for sound risk management.

All rating agencies require cedents to model their largest US terrorism exposures and measure their frequency and severity against their policyholder surplus. Those carriers that have notable backstop TRIA protection as a percentage of their policyholder surplus may benefit from having proactive rating agency discussions while improving the accuracy of their exposure data and modeling output. They may also benefit from proactively pursuing exposure identification, exposure mitigation though portfolio management, and exploring various reinsurance solutions.

IMPLICATIONS FOR MEETING LENDER REQUIREMENTS

Terrorism insurance for real estate companies and construction firms is often required as part of their mortgage agreements; TRIA has offered those companies a mechanism for meeting lender requirements. The impact of not meeting the mortgage requirements varies from client to client and can include minimum premium spends, which are considered punitive. It has been speculated that the absence of TRIA could impact real estate investment and construction/development activity because of the challenge with meeting lender requirements.

Terrorism coverage may still be offered by certain property carriers if TRIA is not extended. However, it is very unlikely this would be at the levels that US businesses, specifically real estate and construction companies — two industries especially susceptible to meeting lender requirements — would need to meet their and their lenders' risk transfer needs. Additionally, there likely would be certain areas where market-wide capacity would be limited. Terrorism capacity/coverage would be at higher cost than businesses are currently paying.

POTENTIAL APPROACHES TO TERRORISM PROGRAMS

For insureds that currently rely substantially on TRIA for terrorism coverage, the current period of uncertainty is problematic. During 2013 and 2014 — or until a decision is made about TRIA's future — a number of approaches can be considered by insureds.

Following are some examples of potential approaches. It is important to note that any program structure needs to be implemented based on an insured's specific needs. Also, in most cases for the buyers of TRIA coverage in areas with the highest demand for terrorism coverage, these approaches are unlikely to completely replace the current level of coverage and limits provided under TRIA as part of property or captive programs.

- Insureds with TRIA 100% embedded as part of "all risk" property programs should work in coordination with property brokers and insurers to determine which property insurers are likely to continue to offer terrorism coverage as part of property programs, regardless of TRIA's extension. If potential gaps in property insurer capacity are identified should TRIA be substantially changed or not extended, insureds likely will have options to consider. For example, they may want to consider placing standalone capacity to fill gaps in capacity. Other alternatives include standalone capacity commitment contracts or excess standalone contracts with the option to drop down and fill gaps in capacity where property carriers cannot continue offering terrorism coverage in TRIA's absence. These approaches are likely to add to the total overall terrorism insurance cost; and in cases where insureds have exposure in major cities or areas where standalone terrorism carriers offer limited capacity, they are likely to result in reduced overall limits and coverage for terrorism.

- Insureds that currently access property TRIA coverage, either as part of a captive property program or as a standalone captive TRIA policy, should consider securing standalone terrorism reinsurance for the captive's liabilities as defined by the Act. This standalone capacity can then be accessed on a direct basis in the event TRIA is not extended.

- Captives providing property TRIA coverage that already purchase standalone terrorism reinsurance, can consider identifying options with standalone terrorism insurers to increase their capacity to cover potential changes in TRIA — such as an increase in the level of reinsurance required. If TRIA is not extended, they can consider converting the standalone terrorism reinsurance limits to primary coverage and seek additional limits in the standalone terrorism insurance market.

- Insureds that currently access standalone terrorism insurance markets for either US noncertified or international terrorism coverage should engage standalone terrorism carriers to discuss various options and terms for converting capacity to cover full terrorism risk in the US, including any foreign or domestic acts that would have been covered under TRIA.

Since both insurers and reinsurers focus on catastrophe models to help determine their underwriting strategies — including whether to offer coverage, the amount of capacity offered, and pricing — it is critical that insureds provide the highest quality of data possible for both property and employee accumulation, as this will help to ensure they receive the most accurate terms, conditions, and pricing based on their actual exposures. There is a direct correlation between high-quality data and the credibility of modeled catastrophic losses and ability to quantify an employer's hazard profile.

Some examples of high-quality data elements that can affect a carrier's view of terrorism loss potential for a particular insured and that can help minimize the impact that default assumptions have on expected modeled losses include:

- Accurate location and property/building information, including COPE (construction, occupancy, protection, and exposure) data.

- Total number of employees by location at the address level.

- Shift information or maximum at each location at any one time.

- Single location or multiple building campus setting.

From a workers' compensation coverage perspective, providing employees by building location in a campus setting will help to mitigate one pitfall of the catastrophic models that defaults to assuming that all employees are in a single building versus being spread across the buildings where they actually work. Identifying the actual buildings where employees work in a campus setting should, when done according to best practices, reduce the loss potential to most types of catastrophic workers' compensation events (for example, terrorism, industrial accident, and natural disasters).

Two other data elements that can make a difference in quantifying an employer's actual hazard profile are construction type and the floor where employees are located. Some building types are less prone to immediate collapse, which gives employees more time to evacuate in catastrophic loss scenarios.

In terms of an insured's property coverage, the more complete the data, the more accurate and comprehensive the CAT models will be. This lack of volatility and uncertainty allows property insurers to more accurately price coverage and insureds to better understand their exposures. As a result, the insured can be better positioned to purchase adequate coverage limits with appropriate terms and conditions.

STEPS FOR CAPTIVES CONSIDERING ACCESSING TRIA

Captive owners and non-captive owners alike should consider initiating or expanding relationships with traditional insurers in order to be in a stronger position to request expanded coverage should it be desired. Captive owners should also ensure the policies their captives write contain appropriate provisions to enable cancellation or modification of terrorism coverage in the event of a material change in or expiration of TRIA.

Until the Act's scheduled expiration on December 31, 2014, using a captive to access TRIA can be a viable option for some companies. Organizations considering using their captives to access TRIA should consider the following recommendations:

- Determine the captive exposure by calculating the 20% horizontal deductible, and the vertical 15% quota-share based on the policy limit.
- Determine the premium to charge for terrorism coverage. US Treasury guidelines state the premiums must not be discriminatory, excessive, or inadequate. If they are found to be so, this could jeopardize the captive's ability to collect in the event of a loss.
- Be aware of, and factor in, the terrorism risks that are not covered by the Act (such as losses occurring outside of the United States).
- Consider purchasing reinsurance for the horizontal deductible, vertical 15% quota-share, and $100 million net trigger liability.
- Consider purchasing coverage for a deliberation or delay in the TRIA certification and/or payment process lasting greater than 180 days.
- Keep in mind that the captive, like all insurers, will be responsible for assessing, collecting, and distributing the post-loss surcharge that will be assessed against all policyholders in the event a loss occurs.
- Compare the findings against commercial insurance options.
- If the decision is made to use a captive, secure the approval of the responsible domicile insurance regulator and implement the program.

POLITICAL ENVIRONMENT

Federal lawmakers will likely address TRIA, which is set to expire on December 31, 2014, during the 113th Congress. Members will have to decide whether to reauthorize the Act as is, amend and modify key provisions, or allow the program to expire. Two key factors will influence the debate:

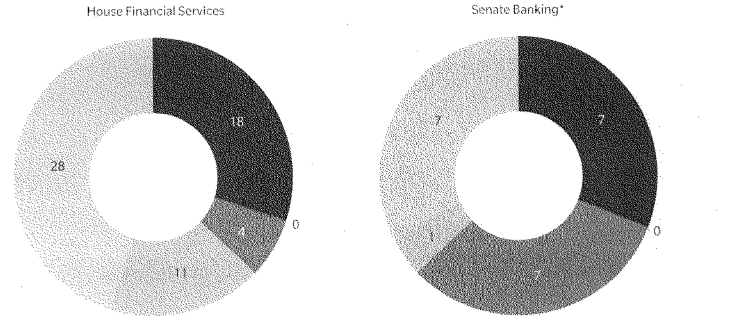
- First, the two congressional committees with jurisdiction over the program — the Senate Banking Committee (SBC) and House Financial Services Committee (HFSC) — have new leaders and members with divergent perspectives on TRIA and its future.
- Second, the composition of Congress has changed considerably since the 2007 reauthorization.

The process will begin in the HFSC, where Republican Jeb Hensarling of Texas, in his new role as chairman, will set the agenda. Of importance to the debate, he and 11 current senior Republican members of the HFSC opposed passage of the 2007 TRIA extension both in the committee and when the entire US House of Representatives voted on the bill in September 2007 (see Figure 14). The voices of the chairman and these 11 senior members will likely carry great weight. New members of the panel will look to their leadership for guidance during the debate. Across the Capitol, Senator Tim Johnson, Democratic chairman of the SBC, likely will preside over a less controversial process. During the 2007 TRIA extension, the bill passed easily in both the committee and in the full Senate.

Both committees have staked out differing views concerning their intent to examine and debate the program. Whereas the SBC's business agenda for the next two years includes language to enact long-term reauthorization of TRIA "with appropriate improvements, as necessary," the HFSC's two-year oversight plan called for expanded deliberation. Indeed, as the oversight plan explicitly points out, the "Committee will examine the private sector's capacity to assess and price for terrorism risk and consider whether to reauthorize TRIA as well as proposals that would reduce the potential federal exposure and participation in the TRIA." This language suggests a straight extension without meaningful reforms may be unlikely. The number of congressional members who were not in office for the 2007 debate complicates matters: 46% of the current HFSC members are new since 2007, as are one-third of the members of the SBC.

On September 11, 2012, the HFSC held a subcommittee hearing in which panel witnesses were in near-unanimous agreement in support of the program and a long-term reauthorization. On February 5, 2013, Representative Michael Grimm (R-NY), a member of the Financial Services Committee, introduced a straight extension of TRIPRA. And President Obama's FY 2014 budget projects net TRIA spending of $443 million over the 2014 – 2018 period and $526 million over the 2014 – 2023 period.

FIGURE 14: CURRENT COMMITTEE MEMBERS AND THE 2007 TRIA REAUTHORIZATION VOTE



* Senator Heller voted against reauthorization while a member of the House

Source: Marsh & McLennan Companies Government Affairs
DEMOCRAT YES · DEMOCRAT NO · REPUBLICAN YES · REPUBLICAN NO · NOT IN CONGRESS

CONCLUSION

For more than 10 years, US-based insureds have benefited from access to terrorism insurance as a result of TRIA. Insureds and insurers alike must prepare for the possibility the Act will be materially changed or allowed to expire on December 31, 2014. Data clearly show a demand for — and a perceived need of — this coverage across many insurance lines, notably property, casualty, and workers' compensation.

Although there is private market capacity for terrorism insurance, it may not be enough to meet the demand in the marketplace should TRIA not be reauthorized. In that case, despite an ongoing exposure to terrorism events, insureds may be unable to secure adequate capacity to insure their risks, or may be unable to do so at commercially viable prices. It is likely that many would be left to self-insure at least some portion of their terrorism risk.

From the standpoint of global business competition, it should be noted that there are a number of countries that offer government supported terrorism risk transfer solutions that are likely to remain available. For these and other reasons, representatives from real estate, finance, energy, construction, insurance, professional sports leagues, and elsewhere have supported TRIA and are making the case for its reauthorization.

APPENDIX

INDUSTRY CATEGORIES

This report examined property terrorism insurance purchasing patterns for 17 industry sectors, selected based on such criteria as sample population size, perceived exposures, take-up rates, and premium rates. Other industry groups were part of the overall analysis but not reported on individually. The industry groupings included, but were not limited to, the following lines of business:

- **Chemicals:** specialty chemicals, agrochemicals, distributors, industrial gases, and personal care and household companies.
- **Construction:** contractors, homebuilders, and general contractors.
- **Education:** universities and school districts.
- **Energy:** oil, gas, and pipelines.
- **Financial institutions:** banks, insurers, and securities firms.
- **Food and beverage:** manufacturers and distributors.
- **Hospitality:** hotels, casinos, sporting arenas, performing arts centers, and restaurants.
- **Health care:** hospitals and managed-care facilities.
- **Life sciences:** research, manufacturers, biotechnology, and pharmaceuticals.
- **Manufacturing:** all manufacturers, excluding aviation.
- **Media:** print and electronic media.
- **Public entity and nonprofit:** city, county, and state entities and nonprofit organizations.
- **Real estate:** real estate and property management companies.
- **Retail and wholesale:** retail entities of all kinds.
- **Technology/telecom:** hardware and software manufacturers and distributors, telephone companies, and internet service providers.
- **Transportation:** trucking and bus companies.
- **Power and utility:** public and private gas, electric, and water utilities.

METHODOLOGY

The report analyses relied on data from Marsh clients that purchased property terrorism insurance across the United States. Purchasing patterns were examined in the aggregate and were also based on client characteristics such as size, industry, and region.

The 2012 data came from property insurance placements incepting during calendar year 2012. The study population does not include placements in the United States for foreign-based multinationals or for small-firm placements made through package policies.

The 2012 study was based on a sample of 2,558 firms with the following characteristics:

	1ST QUARTILE	MEDIAN	3RD QUARTILE
TIV	$36 million	$165 million	$675 million
Property Premium	$51,411	$171,277	$555,495
Terrorism Premium	$1,000	$4,915	$16,409

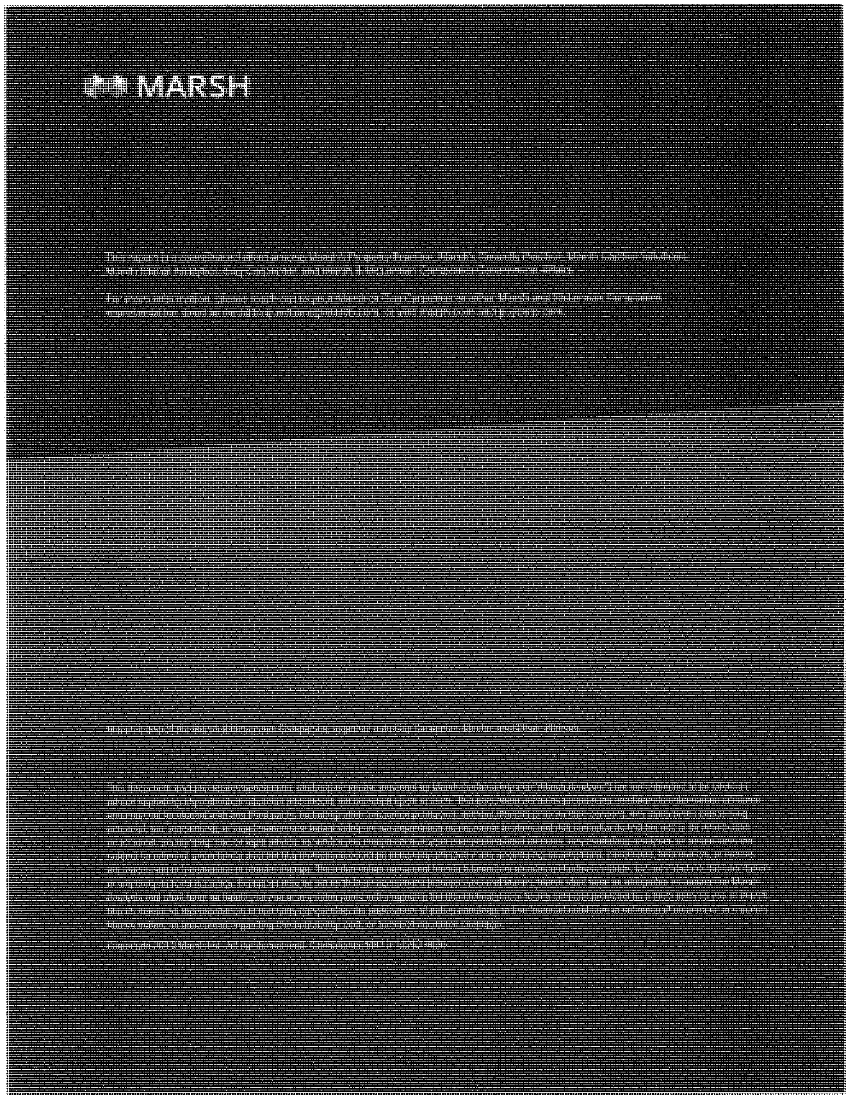
It is important to note:

- The sample size for the energy industry sector was relatively small and therefore may not be statistically significant. There may be a larger margin of error in the data analyzed, which may result in property terrorism take-up rates and pricing for energy companies varying more widely than the data indicates.
- For some companies, insurers quoted only a nominal terrorism premium of $1. These $1 premiums were omitted from the calculations of the median terrorism premium rates.
- Companies were assigned to regions based on the locations of the Marsh offices that served them. Generally, this was the Marsh office most closely located to a company's headquarters. Many clients have multiple facilities across the US and the world, meaning the potential risk for a terrorist attack may not be fully represented by where a company is headquartered. That said, the decision as to whether to purchase terrorism insurance is typically made at headquarters.

NOTES

ABOUT MARSH

Marsh is a global leader in insurance broking and risk management. We help clients succeed by defining, designing, and delivering innovative industry-specific solutions that help them effectively manage risk. We have approximately 25,000 colleagues working together to serve clients in more than 100 countries. Marsh is a wholly owned subsidiary of Marsh & McLennan Companies, whose market-leading professional services companies offer clients advice and solutions in the areas of risk, strategy, and human capital.



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Appendix B: Evolution of TRIA

	TRIA 2002	TRIA Extension 2005	TRIPRA 2007
Termination	December 31, 2005	December 31, 2007	December 31, 2014
Make-available provision	Must make coverage available for certified acts of terrorism on same terms and conditions as for other covered risks	No change	No change
Covered acts	Foreign terrorism in the U.S. and on U.S. interests abroad. Includes an act of war for workers' compensation policies only.	No change	Foreign and Domestic terrorism in the U.S. and on U.S. interests abroad. Includes an act of war for workers' compensation policies only.
Certification level	$5 million	No change	No change
Program trigger	$5 million	$5 million in 2006 (thru March 31, 2006) $50 million in 2006 (after March 31, 2006) $100 million in 2007	$100 million in insured loss in a Program Year
Covered Lines	Commercial property and casualty (P&C) insurance (including excess insurance, workers' compensation and surety insurance)	Commercial P&C insurance (including excess insurance, workers' compensation and directors and officers insurance)	No change
Excluded	• Federal crop • Private mortgage • Financial guaranty • Medical malpractice • Health or life insurance including group life • Flood under NFIP • Reinsurance or retro	Added Exclusions: • Commercial auto • Burglary and theft • Surety • Professional liability • Farm owners multiple peril	No change
Insurer Deductible (% of direct earned premium)	15 percent in 2005	17.5 percent in 2006 20 percent in 2007	20 percent
Federal reinsurance quota share	90 percent in 2002-2005	90 percent in 2006 85 percent in 2007	85 percent
Insurance industry retention for mandatory recoupment	$15 billion in 2005	$25 billion in 2006 $27.5 billion in 2007	$27.5 billion
Cap on liability	$100 billion	No change	No change

Wharton
UNIVERSITY of PENNSYLVANIA

Written Testimony
prepared for a hearing of the

Committee on Banking, Housing and Urban Affairs
U.S. Senate

On

"Reauthorizing TRIA:
The State of the Terrorism Risk Insurance Market"

by

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10:00 a.m.
September 25, 2013

Introduction/Summary

Chairman Johnson, Ranking Member Crapo, distinguished members of Committee on Banking, Housing and Urban Affairs, thank you for inviting me to testify today on "Reauthorizing TRIA: The State of the Terrorism Risk Insurance Market." My name is Erwann Michel-Kerjan. I teach at the Wharton School of the University of Pennsylvania and I am Managing Director of the Wharton Risk Management and Decision Processes Center.

For nearly three decades, the Wharton Risk Center has been at the forefront of basic and applied research to promote effective corporate and public policies for low-probability events with potentially catastrophic consequences (i.e. extreme events) based on an understanding of the decision processes of consumers, firms and public sector agencies (http://www.wharton.upenn.edu/riskcenter/). Our team has published over 20 studies on terrorism risk insurance since 2001 and has been active in discussing findings with top policymakers and industry leaders. I personally took part in a number of discussions with Congress and the Administration at that time that led to the 2005 and 2007 renewals and modification of TRIA.

In the absence of any severe large-scale attack on national soil since 2001, the program has been successful at sustaining a robust terrorism insurance market here in the U.S. Our more recent work which I will discuss here shows that the demand for terrorism insurance from medium and large corporations in the U.S is strong and price inelastic (low sensitivity to price) under current conditions. This also indicates that if one would like to reduce government's involvement in that program by increasing insurers' deductible and/or charging for the federal backstop, this could be done incrementally without disrupting the market much. We know little, however, about small businesses.

Without TRIA, though, American taxpayers might actually end up paying as much after a large terrorist attack through federal disaster relief (which it will be impossible to deny, as taxpayers have become de facto the prime funding source in the aftermath of natural disasters and financial crises alike), if not much more as they would today if insurers lower the capacity they provide when the mandatory requirement expires. There will be an expectation for the federal government to pay for most of the uninsured economic losses. I made this point when I testified before the House on September 11, 2012 but it is worth saying it again.

Since 2008 I have also had the privilege to serve as chairman of the OECD Board on Financial Management of Catastrophes. The Organization for Economic Cooperation and Development (OECD) is an international economic organization of 34 countries, of which the U.S. was a founding member in 1961. It is committed to democracy, market economy, and economic progress and provides a platform to compare policy, experiences, seek answers to common problems, and identify good practices.

The Board advises those 34 governments and the G20 upon request (www.oecd.org/daf/fin/catrisks). Two recent OECD international events brought together for the first time ever the heads of all terrorism risk insurance programs around the world, industry leaders and the intelligence community. Of note, of all countries that have established such programs, none has let theirs expire. Looking at other countries is not only important to be able to exchange notes on possible redesign of TRIA, but more fundamentally because American corporations compete with foreign firms which might have a large part of their assets covered by those terrorism insurance programs under different conditions of price and coverage.

My testimony today will focus on three questions:

1) **How is TRIA currently designed and has it achieved its goal? Is there room as part of the reauthorization process for modifying TRIA without disrupting the market?**

2) **Why have I argued that letting TRIA expire would *increase* taxpayers' financial exposure to terrorist attacks, not reduce it?**

3) **How have other OECD countries addressed the terrorism risk coverage challenge? (something important to know for America's competitiveness)**

SECTION I. WHAT DO WE KNOW ABOUT THE TERRORISM INSURANCE MARKET? NEW EMPIRICAL EVIDENCE

The lack of availability of terrorism insurance shortly after the 9/11 attacks led to a call from some private sector groups for federal intervention. For example, the Government Accountability Office reported in 2002 that the construction and real estate industries complained that the lack of available terrorism coverage delayed/prevented projects from going forward because of concerns by lenders or investors.

In response to such concerns, the Terrorism Risk Insurance Act of 2002 (TRIA) was passed by Congress and signed into law by President Bush on November 26, 2002.[1] This program was originally aimed at providing a three-year temporary measure to increase the availability of risk coverage, but the program has been renewed twice since, in 2005 and 2007. TRIA is now extended up to the end of 2014.

In brief, TRIA requires insurers to offer terrorism coverage to all their commercial clients (a legal "make available" requirement). (Note that residential coverage is not included in this program and it is not clear who would pay for residential losses from terrorism). These firms have the right to refuse this coverage unless it is mandated by state law, as in the case of workers' compensation in most states.

Loss sharing under TRIA is organized as follows: The first layer is provided by insurers through a deductible. That deductible is calculated as a percentage of the direct earned premiums each insurer received in the preceding year from its policyholders for all lines of business covered under TRIA. In order to increase the role of the private market over time, this percentage has increased sharply from 7% in 2003, to 10% in 2004, 15% in 2005, and it has been 20% since 2007—**i.e. nearly tripling over time. For several large insurers, this represents billions of dollars before they receive any federal assistance.** The second layer up to $100 billion is the joint responsibility of the federal government and insurers. Specifically, the federal government is responsible for paying 85% of each insurer's primary losses during a given year above the applicable insurer deductible; the insurer covers the remaining 15%.

Contrary to what is done in other countries (see the review in Section III), the U.S. federal government does not collect any premiums for covering 85% of the insurer's losses above the deductible. It provides insurers with free up-front reinsurance for exposure that would ordinarily require a substantial amount of (costly) capital should the insurers seek protection from the private reinsurance market alone. The "up front" is important here since the U.S. Treasury can recoup part of its payment from insurers over time; they can in turn recoup this amount against all their policyholders, victims of the attack or not.

[1] The complete version of the original Act can be downloaded at: http://www.treas.gov/offices/domestic-finance/financial-institution/terrorism-insurance/claims_process/program.shtml.

Has TRIA Worked as Intended?

The main policy goal of TRIA was to ensure that commercial firms across the nation could access subsidized coverage, and as a result, more companies would purchase this coverage.

Market Penetration Has Increased Substantially. The empirical evidence reveals that this strategy has worked. Market data from the two largest insurance brokers, Aon and Marsh, on their own clients (which tend to be larger firms), indicate that take-up rates for terrorism insurance by large firms has more than doubled, from 27% in 2003 to 58% in 2007, a level that has remained stable since (it is 62% today). These figures have been cited in a number of publications and by my fellow panelists today.

Three important points should be noted about this 62% take-up rate. First, this is not a TRIA take-up rate but combines *all* types of terrorism coverage: U.S. risks only (TRIA only), U.S. risks and non-U.S. risks (clients with foreign values; referred as "TRIA and non-certified"), high risks not covered by the market (referred to as "standalone coverage"), and programs structured as a combination of standalone and TRIA coverage (often done through a captive). Second, these are based on the portfolio of clients of the above two brokers which tend to be medium to large size clients (in other words, these are samples only not the full market). Third, there is a lot of heterogeneity across industries (e.g., take-up rate for media, education, financial institutions is around 80% but only 43% in the energy sector; Marsh, 2013).

While we should certainly feel good about the increase observed in 2003-2006, this also means that probably about 4 out of 10 large corporations in the U.S. don't have coverage against terrorism today. Whether they will be able to sustain a large loss with internal or external capital is an open question Congress might want to analyze further. We need to better understand the demand side of this market. Let's remember that on 9/11 terrorism was included as an unnamed peril in most insurance policies so the take-up rate was virtually 100%.

An important element of the discussion about the future of TRIA is that there has been no analysis in recent years of terrorism insurance penetration for small businesses which constitute a vital part of our economy. They are the most vulnerable to financial shocks.

Decrease in Insurance Cost. The increase in coverage discussed above is partly due to the fact that terrorism insurance prices have continuously decreased since 2003. The median premium for terrorism insurance for middle-size and large firms was down from $57 per million of total insured value in 2004, $42 per million to $37 per million in 2008, then to $25 per million in 2009 (data from Marsh); the 2013 Marsh report shows that prices have continued to decrease for those firms to about $20 per million today. This translates into terrorism premiums representing 3% to 5% of property premium paid by those firms. A 2012 report by insurance broker Aon provides similar information on take-up rates for the twelve months ending March 2012: $20 per million for TRIA coverage only (which translates into an average of about 3.5% of the premium charged for property coverage for TRIA only and about 5% for TRIA and non-certified).

This price decrease is largely explained by the absence of a major attack on U.S. soil since 9/11, thanks to the hard work of our government services here and abroad. It is also explained by the natural effect of competition in insurance markets. The 2013 Boston attack had no impact on terrorism risk insurance markets.

While the surveys from leading brokers have provided a great deal of information about how much coverage their clients purchase and how much they pay for it, they do not say much about how *sensitive* that demand is to changes in terrorism insurance cost. A recent analysis (see sidebar below) utilizes these data to show that terrorism insurance is quite price inelastic. This finding has profound policy implications as Congress contemplates different design changes for TRIA.

Measuring Price Elasticity of the Demand for Terrorism Insurance

In a new study forthcoming in the leading peer-reviewed journal in the field, the *Journal of Risk and Insurance*, we accessed as part of a research partnership with Marsh & McLennan, data on insurance purchases by 1,808 large U.S. corporations operating across the country, and characteristics of insurers providing that coverage.

Combining demand and supply data we can then empirically examine corporate demand for insurance and compare property coverage with terrorism coverage, which has never been done before. (The research was supported by Wharton's Managing and Financing Extreme Events Project, Monash University and DHS's Center of Excellence CREATE at the University of Southern California.)

Corporate demand for terrorism insurance and property insurance are found to be rather inelastic. For those firms that purchase terrorism insurance, the demand for that coverage is found to be *more* price inelastic than their demand for property coverage. Depending on the applied estimation technique used for the analysis, the price elasticity for property coverage ranges from -0.19 to -0.36, while the price elasticity of corporate demand for terrorism coverage ranges from -0.11 to -0.25. At -0.11, this means that **increasing the price of terrorism insurance by 10% will only decrease the quantity of coverage bought by 1.1%.**

As an element of comparison, prior studies of price elasticities of demand for residential flood insurance were found to be as high as -1.55 to -4.48 for flood insurance policyholders who benefit from subsidized rates by the federal government (work by Landry & Jahan-Parvar). In that latter case, increasing insurance prices by 10% would result in a very significant drop as high as 44.8% in coverage. In the corporate world, the elasticity of firms' demand for health insurance spending was found to be to be -0.70—that is, 3 to 6 times more sensitive to price change than demand for terrorism insurance as we found it.

These findings have important implications as we discuss the future of TRIA:

a) Firms that bought that coverage really need/want it. They would keep demanding it even if insurers were to slightly increase the premiums they charge.

b) If TRIA were to be modified and insurers' deductible level were slightly increased from the current 20%, most likely we would not see any impact on the market. Similarly, there was no significant demand change when previous deductible levels had been increased.

c) If TRIA were to be modified so the federal government now charged for the financial protection it currently provides (as is done in a number of other countries), insurers could pass part of this cost to the firms; if reasonable and incremental; most likely this would not result in significant market disruption, either.

Sources: Erwann Michel-Kerjan, Paul Raschky and Howard Kunreuther (in press). **Corporate Demand for Insurance: New Evidence from the U.S. Terrorism and Property Markets.** *Journal of Risk and Insurance.*

Effects of the Federal Intervention on Terrorism Insurance Capacity/Concentration

In another recent study, we performed an economic analysis to evaluate how the supply of an additional unit of coverage differed between terrorism insurance (with government intervention) and property insurance (without it) with TRIA in place. We find evidence that insurers in the U.S. are much less diversified for terrorism coverage than they are for property lines of coverage, and to some extend for other types of catastrophe risks (e.g., wind and flood); meaning that they would more easily provide additional coverage to a client for terrorism risk than for these other risks.

This result can be interpreted in two ways. On the one hand, and as some have argued, there could be "gaming" here[2]: some insurers might be taking on much more terrorism risk with the current free up-front reinsurance from the federal government than they would otherwise, knowing that under TRIA they collect all the terrorism insurance premiums but are responsible for only a portion of the loss.

On the other hand, this also means that insurers have provided much more capacity to this market that they would have done otherwise, which was precisely the intent when TRIA was designed. Given the strong demand for terrorism insurance, this has been an important success of the program.

Source: Erwann Michel-Kerjan, and Paul Raschky, **The Effects of Government Intervention on the Market for Corporate Terrorism Insurance.** European Journal of Political Economy, 2011.

SECTION II. WHY ENDING TRIA WILL INCREASE TAXPAYERS' FINANCIAL EXPOSURE TO TERRORISM LOSSES

Some have said that to limit (or avoid any) additional financial exposure of the federal government given the already historical government deficit, TRIA should be allowed to expire in 2014. Under this logic, market forces would lead to even more capacity being provided to the market and more firms being insured. Losses from a terrorist attack would be covered by firms and their insurers (if they are insured).

While the argument is nice in theory, it totally fails to account for the political reality and the now well-known political economy of catastrophe financing in America.

I have no doubt that the day after a large attack, it will become clear than many firms are uninsured or poorly insured because insurers would not be required to offer that coverage anymore and the price of that coverage without a free up-front federal backstop will simply be much higher than it is today to reflect the cost of capital insurers have to set aside to meet regulatory and rating agencies requirements (unless insurers cap their coverage to what they currently cover under their deductible and quota-share above).

Under extreme pressure from the media and interest groups, the federal government will be asked to step in. Americans taxpayers will de facto pay for most of the loss. This outcome is pretty certain as one looks at how much more involved the federal government has been at providing financial support after catastrophes and crises in the past decade than it used to be 50 or 60 years ago. If the attack occurs during an election year, this would be even more certain.

[2] President's Working Group on Financial Markets, Market Conditions for Terrorism Risk Insurance, 2010. See also: Wharton Risk Center (2005). TRIA and Beyond. Philadelphia, PA; Kunreuther, H. (2007), Testimony before the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises of the House Financial Services Committee, June 21.

Overall, the number of Presidential disaster declarations has dramatically increased over time, from 191 declarations over the decade 1961-1970 to 597 for the period 2001-2010. As Figure 1 also reveals, many of the peak years correspond to presidential election years. In 1996 and 2008 (both presidential election years) there were 75 presidential declarations. This record number was exceeded in 2010 when there were 81 major disaster declarations, and again in 2011 with 99 declarations.

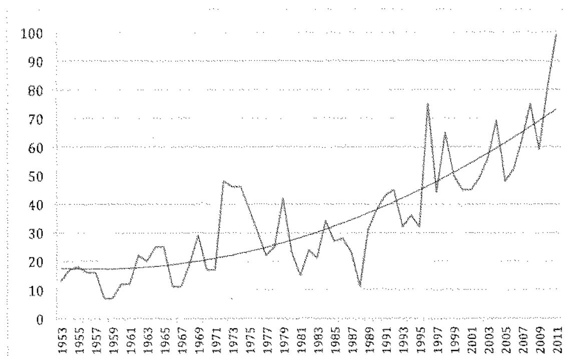


Figure 1. U.S. Disaster Presidential Declarations Per Year, 1953-2011 (data from FEMA)

And it is not just the number of declarations that has increased but the proportion of economic losses that American taxpayers are forced to pay. Table 1 shows the much more pronounced role of the federal government in assisting disaster victims and governments of affected areas by examining several major disasters occurring in the past 60 years. The most recent example is Hurricane Sandy: the federal government provided $50 billion in emergency funds and another $10 billion to the NFIP so it could pay all its claims—that is, 88% of the $68 billion loss from Sandy.

Table 1: Role of Federal Government in Disaster Loss Payment

Disaster	Federal contribution to total loss payment
Hurricane Sandy (2012)	88%
Hurricane Ike (2008)	69%
Hurricane Katrina (2005)	50%
Hurricane Hugo (1989)	23%
Hurricane Diane (1955)	6%

This radical increase in government funding—combined with the highly mediatized bail-out of large American corporations during the recent financial crisis—is likely to set precedents and expectations of more funding to come in the future. This will be especially true for terrorism since it might be seen as a failure of our government services to prevent the attack. **The question thus is how do we best organize risk financing mechanisms ex ante so most of the loss does not fall on taxpayers; under its current design, this is what TRIA does. Reforms should seek to increase the private sector's involvement without disturbing the market.** As I said before, I think there is room to do just that.

SECTION III. TERRORISM INSURANCE SOLUTIONS OUTSIDE OF THE U.S.

In this last section of my testimony I would like to provide some international perspective. While this has been somewhat absent in recent discussions about TRIA, this is important for several reasons: a) Terrorism threat is international by nature; b) Other countries are facing similar challenges as to how best use the strengths of the private and public sectors in developing a robust insurance scheme; c) Many large American corporations generate a significant part (if not the majority) of their revenues abroad and d) American firms compete with foreign firms which benefit from those programs in their home countries.

I will briefly highlight the solutions currently in place in five other countries that have suffered from terrorist attacks on their soil: Israel, Spain, France, the U.K. and Germany (chronologically, as they developed their program). I would like to thank the heads of programs discussed here for ongoing discussions and their insights in preparation of today's testimony. A visual comparison is then provided with Australia and India added in Appendix 1.

Of note, several of these programs are permanent in nature; those that are temporary have all been renewed with some modifications in recent years.

Israel: Government Coverage, No Involvement of Private Insurers

In this country with a long history of terrorist attacks, losses from attacks are compensated directly by the State according to a pre-defined formula. Any direct and indirect damage occurring within Israel due to war or hostilities will be covered by a *public compensation fund* legislated in 1961. The fund built from the general property tax collected across the conntry, according to regulations. Insurers do not cover this risk. Both individual and business compensation is provided to those who suffer from an attack. Businesses can also get compensated for workers' compensation and loss of business revenues.

Renewal and Government Exit Strategy. **The program is permanent.■**

Spain: Government Coverage Sold by Private Insurers in its Behalf

Eligibility. Terrorism has been covered as part of the State-backed insurance compensation scheme for extraordinary risks (including also storms, floods, earthquakes, riots), by the 1954-established *Consortio de Compensation de Seguros* fund. Coverage for these risks is included as an add-on to property insurance sold by private insurers who are not financially responsible for losses. The private sector has never expressed an interest in covering terrorism or these other extreme events. *Pricing.* Commercial enterprises pay 0.21 euros per thousand of property coverage and another 0.25 euros for business interruption to benefit from this state insurance against extraordinary risks.

Loss History. In the aftermath of the March 11, 2004 terrorist attacks in Madrid, the Consortio paid 41 million euros in claims (railway vehicles were not insured). The December 2006 attacks against the Barajas Airport triggered another 46 million euros in claims. These claims were rapidly paid by the Spanish catastrophe fund which currently has over 4 billion euros in reserve and has never used the State guarantee in over 50 years of operation.

Renewal and Government Exit Strategy. **The program is permanent. ■**

France: Public-Private Risk Sharing; Unlimited Government Reinsurance

From a legal perspective, the situation in France was especially acute in the aftermath of 9/11 because the 1986 law does not allow commercial property insurers to dissociate terrorism coverage from commercial property. To stop covering terrorism meant to stop covering commercial property at the 2002 renewals.

The GAREAT, a public-private partnership, was established in December 2001 as a co-reinsurance pool organized under a tier structure of risk sharing. It operates on an aggregate annual excess of loss basis.

Risk-Sharing Arrangement. The first layer presents an annual aggregate capacity of 400 million euros shared among all 205 members of the pool prorated to their share of ceded business. A second layer is provided by members (private insurers) and reinsurers up to 2.3 billion euros. Above that, the State layer is an *unlimited* guarantee by the French government provided through the Caisse Centrale de Reassurance (CCR), a state-owned reinsurance company. Since 2005, there is a special treatment for small risks (below 20 million euros of total insured value): the government grantee is triggered above 20 millions, GAREAT being responsible for the first 20 million euros.

Eligibility. Terrorism insurance is mandatory in France, so the take up rate is 100%. As of 2013 90% of the large commercial and industrial risks had been transferred to the pool and 12% of small risks for property damage and business interruption, including chemical, biological, radiological and nuclear (CBRN) attacks (GAREAT does not cover liability risks, personal accident, marine). Moreover, the same deductible is applied for terrorism as for other property coverage risk pricing.

Pricing. Reinsurance rates by the GAREAT do not vary with location: they are identical across the country. They apply as a percentage of the property premiums of the business ceded for different insured value segments: below 6 million euros (Automobile 0.10%; Homeowners 0.8%; Commercial and Industrial risks 1.20%; Farms: 0.60 %); between 6 million and 20 million euros the rates are 4% for each class of business. For sum insured above 20 million euros: 12% (between 20 and 50 million euros); 18% (sums insured higher than 50 million euros). For nuclear plants the rate is 24% whatever the sum insured are. GAREAT redistributes premiums collected from its members back to them if not used to pay claims.

Premium Sharing with the Government. The premiums levied by insurers against policyholders are transferred to the GAREAT and shared as follows: members of the pool keep nearly 44%, the reinsurance layers 44%, and the CCR receives around 12% of the total annual premiums collected.

Renewal and Government Exit Strategy. The pool was first set up for a single year with the option of being renewed, as was done in 2003 until December 31, 2012. **The program was renewed on January 1, 2013 for another 5 years. ■**

U.K: Public-Private Risk Sharing; Unlimited Government Debt Issuance

In the wake of the terrorist bomb explosions in London in April 1992, which cost insurers nearly $700 million, and an announcement seven months later by British insurers that they would exclude terrorism coverage from their commercial policies, the U.K. established a mutual reinsurance organization, Pool Re, in 1993 for commercial property and business interruption to accommodate claims resulting from acts of terrorism.

Eligibility. The scale of 9/11 attacks in the U.S. led to a major revamping of Pool Re. Since the end of 2002, protection of companies operating in the U.K. under Pool Re has been extended to all risks, a category that now includes damage caused by chemical and biological as well as nuclear contamination (while war and related perils as well as computer hacking continue to be excluded).

Risk-Sharing Arrangement. Pool Re acts as a reinsurer for all insurers that wish to be a member of the pool; the U.K. Treasury in turn provides Pool Re with unlimited debt issuance that the pool will have to reimburse over time. Pool Re's right to draw funds under the retrocession agreement with the government is determined on a strict cash needs basis. That means that premium income earned by Pool Re during the time necessary for claims settlement, i.e. after a terrorist attack, will also be used to pay these claims, if necessary.

All insurers authorized to insure losses arising from damage to commercial property in Great Britain are eligible to apply for membership of Pool Re, regardless of their domicile. Most insurers operating in the U.K. commercial property market are members. As of September 2013, Pool Re has 221 members (73 insurers incorporated in the U.K., 37 Lloyd's syndicates, and 111 insurers incorporated elsewhere). They have an individual retention before being reimbursed by the pool which is based on their proportion of participation in Pool Re, applied to the "industry retention" (£100 million per event, £200 million per year in 2012).

As of September 2013, Pool Re has a reserve of nearly £5.0 billion, which would have to be exhausted before the British Treasury pays anything. If the government needs to intervene for insured losses above this, it will be reimbursed for that payment by the pool over time; and ultimately, the members of Pool Re will have paid *all* insured losses due to the terrorist attack.

Premium sharing with the government. Pool Re shares 10% of its collected premiums with the U.K. government to benefit from this coverage.

Renewal and Government Exit Strategy. Pool Re is not reviewed on any specific cycle, unlike TRIA. The contract has cancellation arrangements whereby either Pool Re or Government can withdraw (with notice, and conditions) but **no pre-set review period, or sunset in the legislation** ■

Germany: Public-Private Risk Sharing; Limited Government Reinsurance

As in other countries, until the events of 9/11, coverage against terrorism risk was included in all commercial lines in Germany without an explicit extra premium. After 9/11, the extremely limited availability of terrorism coverage led to the founding of Extremus AG, a federal government-backed property insurance corporation that started operations on November 1, 2002. Unlike Pool Re, Extremus is not a reinsurance institution but a private insurance company.

Eligibility. Extremus provides coverage for buildings, contents, and business interruption. But only risks with total insured value over 25 million euros are eligible for coverage. As in the U.S. and the U.K., companies operating in Germany are not required to purchase insurance against terrorism. The annual compensation by Extremus for any company is capped at a maximum of 1.5 billion euros. This means that a company with a total insured value of 25 billion euros can purchase coverage for only 6% of its total insured value from Extremus. A number of risks are explicitly excluded, such as nuclear risks as well as biological and chemical contamination by terrorists, war and civil war, and insurrection. Losses due to computer viruses are also not covered. ■

Risk-Sharing Arrangement. The annual capacity to pay for claims is 10 billion euros. It is completely reinsured by national and international insurance and reinsurance companies (first layer limited to a total of 2 billion euros), as well as by the federal government (second layer of 8 billion euros). As of December 31, 2010, Extremus provided a total of 450 billion euros terrorism insurance coverage to 1,174 firms.

Premium Sharing with the Government. As is the case in France and the U.K., but not in the U.S., the reinsurance provided to Extremus by the federal government is not free of charge: the government receives approximately 12.5% of the premiums collected by Extremus.

This international review shows that different countries have responded to the question of terrorism risk financing differently, and that those responses were often modified after terrorist attacks on national soil.

Conclusion

Coming back to United States, several questions will be important as we now discuss the role that TRIA should play in the future, in a world where the nature of terrorism threat is in constant evolution. For instance;

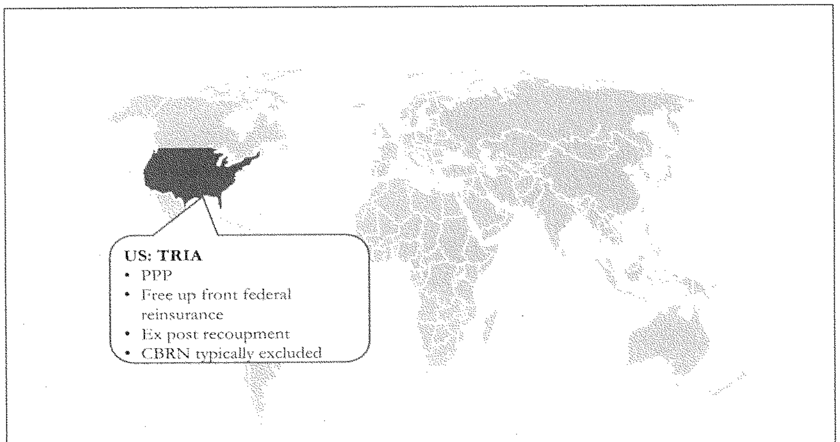
- Should CBRN terrorist attacks (chemical; biological; radiological and nuclear) be covered or not?
- Should cyber attacks be covered and if so, which ones?
- Should our federal government continue to provide free coverage or should it charge for it? If so, what would be seen as a "fair" premium?
- How involved are reinsurers in the U.S. terrorism risk insurance markets today? How much more capacity could they provide, at what level, and at what price? How is reinsurance capacity and price likely to change in the aftermath of a large terrorism attack?
- While TRIA focuses on commercial lines, who will pay for the losses to residents from a terrorist attack?
- How do we address the workers' compensation challenge if TRIA expires?

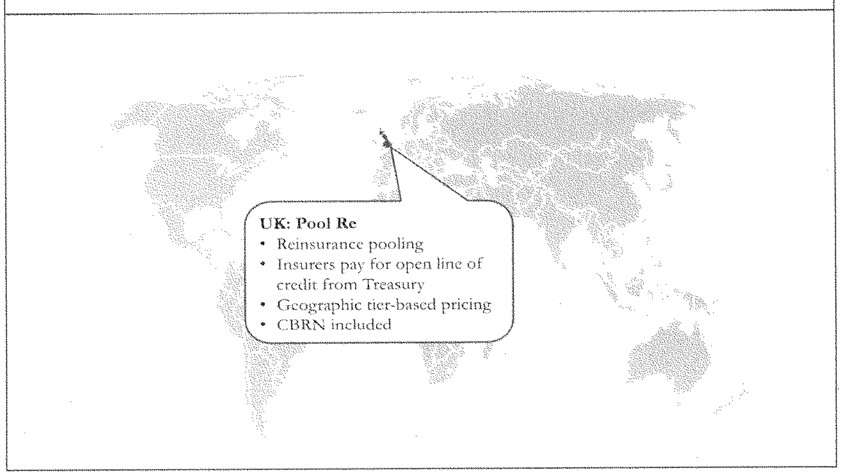
In the end, it is how we best use the insurance infrastructure, in partnership with the government, to assure effective and equitable solutions are in place that will make our economies terror-proof. This is why the debate about TRIA is not just an insurance issue—it is as much a national security and economic competitiveness issue, too.

My colleagues and I look forward to working with Congress, the Administration, the insurance and reinsurance industry and other stakeholders in the near future.

I want to thank you again for the opportunity to testify here today. I would be happy to answer any question you may have.

Appendix 1. Terrorism Insurance Markets in Selected Countries (Sources: Author)[3]





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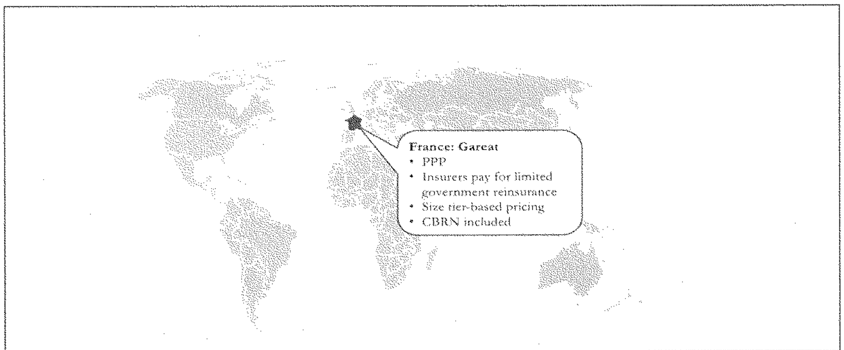
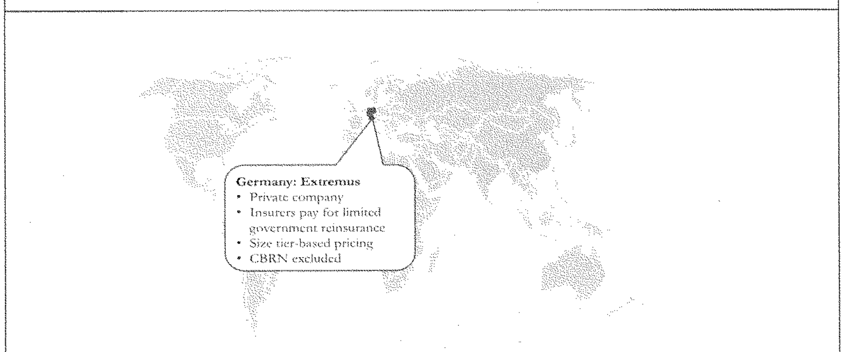
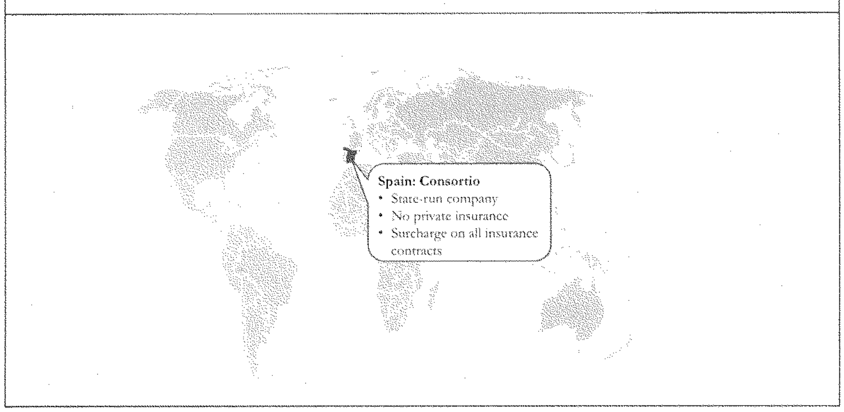
[3] For more on international terrorism risk insurance markets, see:

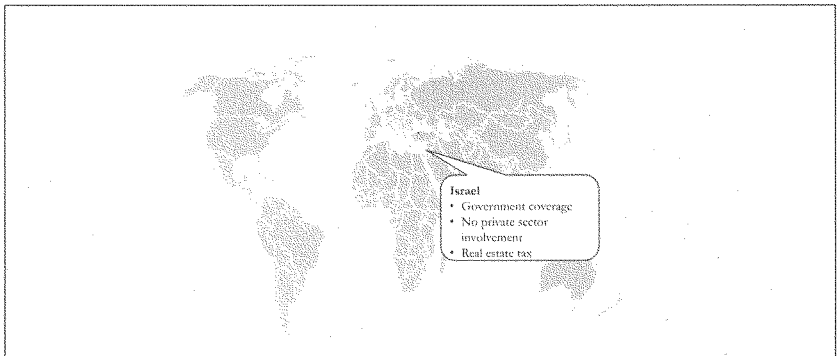
- Michel-Kerjan, E. and B. Pedell. (2006). How Does the Corporate World Cope with Mega-Terrorism? Puzzling Evidence from Terrorism Insurance Markets. *Journal of Applied Corporate Finance*, 18(4):61-75.
- OECD. Terrorism Insurance in OECD Countries, 2005;
- OECD. Terrorism Insurance in 2010: Where Do We Stand? Proceedings of the June 2010 conference, Paris;
- OECD. Terrorism Risk Insurance Markets in 2012.

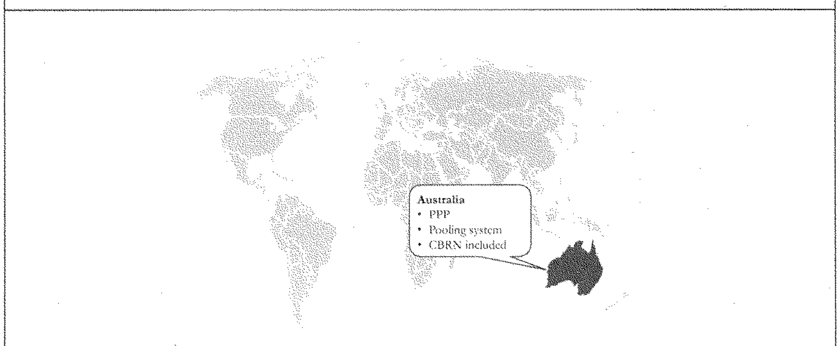
Please visit: www.oecd.org/daf/fin/catrisks

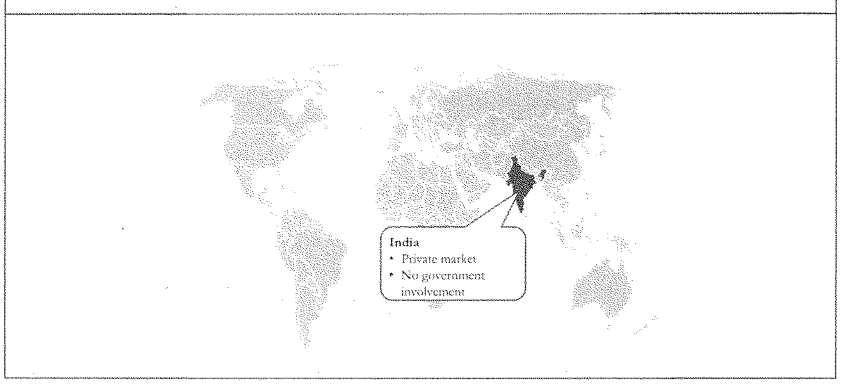

France: Gareat
• PPP
• Insurers pay for limited government reinsurance
• Size tier-based pricing
• CBRN included


Germany: Extremus
• Private company
• Insurers pay for limited government reinsurance
• Size tier-based pricing
• CBRN excluded


Spain: Consortio
• State-run company
• No private insurance
• Surcharge on all insurance contracts


Israel
• Government coverage
• No private sector involvement
• Real estate tax


Australia
• PPP
• Pooling system
• CBRN included


India
• Private market
• No government involvement

Reauthorizing TRIA:
The State of the Terrorism Risk Insurance Market

United State Senate
Committee on Banking, Housing and Urban Affairs

Testimony of
Robert P. Hartwig, Ph.D., CPCU
President & Economist
Insurance Information Institute
New York, NY

September 25, 2013

Washington, DC

Thank you, Senator Johnson, Ranking Member Crapo and members of the Committee.

Good morning. My name is Robert Hartwig and I am President and Economist for the Insurance Information Institute, an international property/casualty insurance trade association based in New York City.[1] I am also a Chartered Property Casualty Underwriter (CPCU) and have worked on a wide variety of insurance issues during my 20 years in the property/casualty insurance and reinsurance industries, including many related to the industry's exposure to catastrophic loss, including acts or terrorism.[2] The Institute's members account for nearly 70 percent of all property/casualty insurance premiums written in the United States. Its primary mission is to improve understanding of the insurance industry and the key role it plays in the U.S. and global economy.

I have been asked by the Committee to provide testimony on the current state the Terrorism Risk Insurance Program and the market for terrorism insurance in the United States. For the purposes of my testimony, I will address the following issues:

(i) The immediate impacts of the September 11, 2001 attacks on insurance and reinsurance markets;

(ii) The essential role that TRIA plays with the nation's national security infrastructure and its benefits to consumers, businesses and communities;

(iii) Taxpayer protection features of TRIA;

(iv) Private sector insurer and reinsurer involvement in terrorism insurance markets since 9/11;

(v) The unique nature of terrorism risk and the limits of private sector involvement in terrorism insurance markets;

(vi) Changes in the terrorism threat landscape since the enactment of the original TRIA legislation in 2002 and the impacts on terrorism insurance;

(vii) Potential economic and insurance market impacts if TRIA is not extended;

(viii) Obstacles to insuring and reinsuring losses arising from acts of terrorism;

(ix) Cyber terrorism and certification timelines.

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[1] Contact information: Tel: (212) 346-5520; Email: bobh@iii.org.

[2] See *Terrorism Risk: A Constant Threat*, Robert P. Hartwig and Claire Wilkinson, Insurance Information Institute, June 2013.

Impacts of the September 11, 2001 Terrorist Attack on Insurance Markets

The terrorist attacks of September 11, 2001, produced insured losses larger than any natural or man-made event in history. Claims paid by insurers to their policyholders eventually totaled some $32.5 billion dollars—$42.1 billion in 2012 dollars (Exhibit 1) and to this day remains the second most costly insurance event in United States history (Exhibit 2).[3] The insured losses arising from the events of that fateful day were unprecedented in virtually every respect, producing catastrophic losses not only in property coverages, but also for the first time in the workers compensation line. The sheer enormity of the loss—coming from an entirely unforeseen peril for which no premium had been collected—combined with the possibility of future attacks, produced financial shockwaves that shook insurance markets worldwide and provoked an extraordinarily swift and severe underwriting and pricing reaction by insurers and reinsurers.

Terrorism Exclusions and Price Shocks in the Wake of the 9/11 Attack

The shock of the September 11 attack led insurers and reinsurers to exclude coverage arising from acts of terrorism from virtually all commercial property and liability policies. Before 9/11 terrorism exclusions were virtually nonexistent in commercial insurance contracts sold in the United States. The economic consequences of such exclusions were quick to manifest themselves. Major commercial property construction projects around the country, unable to secure coverage against the now very real risk of terrorist attack, were in jeopardy of being tabled, hurting job growth at a time of rapidly rising unemployment and when much of the country was in recession. Banks, in turn, threatened to choke off lending to businesses if borrowers failed to secure coverage against terrorist acts. The problem was not confined to high profile "trophy" properties located in major metropolitan areas. Shopping malls, office complexes, factories, sports stadiums, hotels, utilities, airports, port facilities and other critical infrastructure all across the United States were impacted. In short, the macroeconomic consequences associated with the lack of terrorism coverage were beginning to exact a severe toll on businesses

[3] The loss totals do not include the March 2010 settlement of up to $657.5 million announced by New York City officials and plaintiffs' lawyers to compensate about 10,000 workers whose health was damaged during the rescue and cleanup at the World Trade Center.

and workers alike. *[Note: The potential macroeconomic implications of allowing TRIA to expire in 2014 are discussed in greater detail in the next section of this paper].*

Even as exclusions proliferated, prices soared. The average rate increase for a business seeking to renew coverage in the fourth quarter of 2001 was nearly 30 percent. Reinsurance prices rose sharply as well. Very little private sector coverage for terrorism entered the market as a general consensus emerged that terrorism risk is fundamentally not insurable. Insurers, who are regulated by the states, therefore took the unprecedented step of seeking to establish a risk sharing plan with the federal government in the event of future attacks. Only when the Terrorism Risk Insurance Act (TRIA) was enacted by Congress in November 2002—fourteen months after the attack—did stability finally return to the market and coverage for terrorist attacks resume.

TRIA, National Security and Protection of the Nation's Critical Financial Infrastructure

The war on terror is far from over, as the recent Boston Marathon bombings attest, but TRIA by all objective measures is now a proven and unqualified success. The program not only succeeded in restoring stability to the country's vital insurance and reinsurance markets in the years immediately following 9/11, but it continues more than a decade later to deliver substantive, direct benefits to millions of businesses, workers, consumers and the overall economy—all at essentially no cost to taxpayers.

Upwards of 60 percent of businesses purchased terrorism coverage nationally in 2012, up from 27 percent in 2003, the first full year of the program (Exhibit 3). Industries responsible for much of the country's critical infrastructure such as power and utilities, telecommunications and health care, along with financial institutions and local government have take-up rates that approach or exceed 70 percent. Moreover, the take-up rate for workers compensation is effectively 100 percent, meaning that every worker in America is protected against injuries suffered as the result of a terrorist attack.

The unambiguous success of TRIA demonstrates that the Act has become an invaluable component of the country's national security infrastructure. The continued operation of the nation's financial institutions—including its insurers—during and throughout the aftermath of a major terrorist attack—is absolutely essential to ensure a smooth and expedited recovery from the massive economic and operational shocks of the sort that occurred after the 9/11 attacks and that are certain to accompany future such events, irrespective of where in the country they occur. Failure to institutionalize a permanent plan to protect the nation's financial infrastructure leaves the country unnecessarily vulnerable to economic instability and risk of recession.

Macroeconomic Impacts of the TRIA Expiration

A 2004 study co-authored by R. Glenn Hubbard, Columbia University's Business School Dean and a former chairman of the U.S. Council of Economic Advisors, quantified the potential macroeconomic impacts of a failure to extend TRIA.[4] The study concluded that within three years of the expiration of TRIA (in the absence of a major terrorist attack), GDP could fall by 0.4 percent, household net worth by 0.9 percent and employment by 0.2 percent. Applying the findings of that study to the current period suggests that expiration of the current Act could lead to a meaningful drag on economic growth, reducing real GDP by an estimated $69 billion by 2017, depressing household net worth by an estimated $798 billion and remove 290,000 jobs from the economy.[5]

Table 1

POTENTIAL MACROECONOMIC IMPACTS ASSOCIATED WITH THE EXPIRATION OF TRIA

Macroeconomic Factor	Estimated Impact Within 3 Years of Terrorism Program Expiration
Real GDP	-$69 Billion
Household Net Worth	-$798 Billion
Jobs	-290,000

[4] R. Glenn Hubbard and Bruce Deal, *The Economic Effects of Federal Participation in Terrorism Risk*, Analysis Group, September 14, 2004.
[5] Figures cited in Table 1 are Insurance Information Institute estimates based on findings of the study referenced in footnote 3.

As Table 1 demonstrates, terrorism remains a threat to the country's national economic security, especially in the context of the still fragile economic recovery. Consequently, maintaining a Terrorism Risk Insurance Program as a component of the country's comprehensive national security plan and infrastructure is both reasonable and prudent. It is also imminently affordable. Indeed, the cost to American taxpayers is effectively zero.

Taxpayer Protection Features of the Terrorism Risk Insurance Act

TRIA from its inception was designed as a terrorism risk sharing mechanism between the public and private sector—with an overwhelming share of the risk being borne by private insurers, a share which has increased steadily over time. Today, all but the very largest (and least likely) terrorist attacks would be financed entirely within the private sector. In the event of a truly catastrophic attack, TRIA provides the government with the ability to fully recoup any and all federal monies paid. In other words, there would be *no* cost to the taxpayer.

As a point of fact, from the date of TRIA's enactment in November 2002 through today, a span of nearly 11 years, the federal government and therefore taxpayers have paid nothing (apart from negligible administrative expenses) under the program. The recent Boston Marathon bombings provide an illustrative example. All of the 207 property/casualty claims filed in the wake of that event were handled by private insurers who have made payments to policyholders totaling at least $1.18 million.[6] Not one taxpayer dollar was used to pay any of these claims.

TRIA's structure actually provides at least eight distinct layers of taxpayer protection as displayed schematically in Exhibit 4's Pyramid of Taxpayer Protection. Each of those layers is discussed in turn below.

[6] As of July 26 (latest available). P/C insurers also held $1.41 million in reserves for claims associated with the bombings. Figures are from the Massachusetts Division of Insurance as reported in BestWire Services, *P/C Insurers Have Paid $1.18 Million in Boston Marathon Bombing Related Claims*, September 3, 2013.

SUMMARY OF 8 KEY TAXPAYER PROTECTION FEATURES UNDER TRIA

1. **CERTIFICATION DEFINITION:** ***Criteria Must Be Met***[7]
   - **Definition of a Certified Act of Terrorism:** The 2007 extension of TRIA, likes its predecessors, requires that a detailed set of criteria be met before an act of terror can be "certified." Specifically, the term "act of terrorism" refers only to an act that is certified by the [Treasury] Secretary, in concurrence with the Secretary of State and the Attorney General of the United States:
     i. to be an act of terrorism;
     ii. to be a violent act or an act that is dangerous to human life, property or infrastructure;
     iii. to have resulted in damage within the United States, or outside of the United States in the case US air carriers, vessels and/or missions;
     iv. to have been committed by and individuals as part of an effort to coerce the civilian population of the United States or to influence the policy or affect the conduct of the US government by coercion.

2. **CERTIFICATION THRESHOLD (TRIGGER):** ***$5 Million***
   - **$5 Million Minimum:** Under the 2007 reauthorization of TRIA, no act shall be certified by the Secretary as an act of terrorism if property and casualty losses, in the aggregate, do not exceed $5 million.
   - **Acts of War Exclusion:** TRIA further stipulates that no act may be certified as an act of terrorism if the act is committed as part of the course of a war declared by Congress (this provision does not apply to workers compensation).

3. **TRIGGERING EVENT THRESHOLD:** ***$100 Million***
   - Under the 2007 reauthorization of TRIA the triggering event threshold was set at $100 million, up from $5 million in the original act and $50 million in 2006. This means that Federal funds will be paid out *only* in the event of a terrorist act that produces total insurance industry losses above this threshold (even if the event is certified by the Treasury Secretary as a terrorist act).

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[7] United States Treasury accessed as of 9/22/13 at http://www.treasury.gov/resource-center/fin-mkts/Documents/TRIAasamended-CompositeTextPost.pdf.

4. **INDIVIDUAL INSURER DEDUCTIBLES:** ***20% of Premiums***
   - The amount of terrorism losses that an individual insurer must pay before federal assistance becomes available. The level rose to 20 percent of an insurer's direct earned premiums for commercial property/casualty insurance in 2007 where it currently remains (up from 17.5% in 2006, 15 percent in 2005, 10% in 2004 and 7% in 2003).

5. **INSURER CO-PAYMENT IN EXCESS OF RETENTION:** ***15% of Loss***
   - The share of losses that insurers pay above their individual retentions rose to 15 percent in 2007 where it remains today, up from 10 percent in 2006 and prior years.

6. **INDUSTRY AGGREGATE RETENTION:** ***$27.5 Billion***
   - Under the 2007 reauthorization, the industry as a whole must ultimately cover a total of $27.5 billion of the losses through deductibles and copayments (assuming an event of $27.5 billion or greater). This amount was increased to $27.5 billion in 2007, up from $25 billion in 2006, $15 billion in 2005, $12.5 billion 2004 and $10 billion in 2003 ***(Figure 7)***. Government expenditure above this amount can be recouped.

7. **GOVERNMENT RECOUPMENT:** ***Full Taxpayer Protection***
   - **Mandatory Recoupment:** TRIA mandates that the government recoup *133 percent* of the difference between the actual amount it has paid and the required retention. This recoupment comes via a surcharge on commercial insurance policyholders not to exceed 3 percent of premium for insurance coverages that fall under the program.
   - **Discretionary Recoupment:** If the insured loss exceeds the $27.5 billion threshold, federal expenditures may be recouped for amounts in excess of the threshold at the discretion of the Secretary of the Treasury.

8. **HARD CAP:** ***$100 Billion***
   - **Program Limit:** Losses within a program year are capped at $100 billion, inclusive of both insurer and government participation. Neither the government nor insurers would be required to pay losses for certified acts beyond this amount.

Additional Taxpayer Protection Features of TRIA

Several other features of TRIA serve as additional protections to taxpayers.

Commercial Lines Only: Only claims occurring in certain property/casualty commercial lines of insurance are included in the calculations of insured losses under TRIA (auto and homeowners insurance, life insurance and health insurance have always been excluded). In addition, the number of lines covered under TRIA has been narrowed over time. At TRIA's inception in 2002 approximately 44 percent of property/casualty insurance industry premiums were covered under the Act. By 2012 that figure had dropped to approximately 35 percent. Excluded commercial lines of coverage under the Act today include: mortgage and title insurance, financial guaranty, medical malpractice, reinsurance, commercial auto, burglary and theft, surety, professional liability (except directors and officers coverage) and farmowners multiperil.

State Guaranty Funds: In the unlikely event that an insurer becomes severely impaired or insolvent as a consequence of a terrorist attack, state insurance regulators will take corrective action. If the insurer's assets are insufficient to meet its liabilities, the resources of the appropriate state guaranty fund(s) could be called upon to satisfy those liabilities. Guaranty associations obtain funds for their operations and payment of claims through assessments against the solvent insurance companies licensed to do business in the state and from the recovery of amounts paid on claims from the insolvent estate.[8] All guaranty fund resources are therefore ultimately derived from the industry itself. *No taxpayer dollars are ever involved.*

Make Available Requirement (Mandatory Offer of Coverage): Commercial insurers are required to offer coverage against terrorist acts and by law, workers compensation must include coverage against such acts. These requirements have led to widespread participation in the program. The take-up rate for terrorism coverage in 2012 was 62

[8] National Conference of Insurance Guaranty Funds accessed September 22, 2013 at: http://www.ncigf.org/media/files/Primer-2012.pdf

percent according to a recent study by insurance broker Marsh.[9] The take-up rate for workers compensation is effectively 100 percent, meaning that every worker in America is protected against injuries suffered as the result of a terrorist attack.

TRIA Will Reduce Taxpayer Funded Post-Attack Disaster Aid Costs

The very fact that terrorism coverage is so widely purchased today and that coverage already extends to every American worker through the workers compensation system means that fewer government (taxpayer) resources will be called upon in the wake of any future terrorist attack. Allowing TRIA to expire will reduce the market penetration of terrorism coverage as prices rise and insurers limit their exposure across all lines of coverage, including workers compensation. Consequently, the uninsured share of losses will rise, increasing the pressure on the government to compensate victims for their uninsured losses. This will impair the ability of individual businesses, affected communities and the overall economy's ability to recover. A sharp spike in business failures, higher unemployment and reduced GDP growth are just a few of the adverse consequences that are certain to follow in the event of a major terrorist attack in the absence of TRIA. In summary, government will be called upon to act in the aftermath of a major terrorist attack. TRIA provides an efficient means for ensuring that most of the costs are financed and administered by the private sector rather than the taxpayer.

Use of Insurer Claim Management Infrastructure Will Save Taxpayer Money, Improve Post-Attack Response

Private insurers are today the principal source and conduit for the rapid and direct delivery of recovery funds to victims of terrorist attacks. In the event that TRIA is allowed to expire, the government lacks any formal structure or experience for adjusting, managing and delivering benefits to victims of complex commercial property and liability claims, nor does it have any formal fraud monitoring capability. Maintaining TRIA not only ensures that the costs of future terrorist attacks will be borne primarily by the private sector, it enhances the quality of the outcome. Again, in the absence of TRIA there is no question that the federal government will be called upon to act. TRIA ensures that that much of those costs will be borne and administered by the private insurers.

[9] Marsh, *2013 Terrorism Risk Insurance Report*, May 2013.

Private Insurer and Reinsurance Participation in the Market for Terrorism Insurance Today

One primary goal of TRIA and it successors has been to encourage private sector capacity to enter (and remain) in the marketplace so that an increasing share of losses from future terrorist attacks could be borne in the private sector.

There is no question that billions of dollars in capacity has been attracted to the terrorism risk insurance market. Evidence of the program's success in this respect has been documented by a number of government entities and other organizations. In its latest report on terrorism risk insurance market conditions, the President's Working Group on Financial Markets noted that the program provides an incentive to property/casualty insurers and reinsurers who might not otherwise provide terrorism insurance at current capacity levels or prices.[10] The U.S. Government Accountability Office (GAO), commenting on the availability and affordability of terrorism coverage in large metropolitan areas, reported that with a few exceptions, commercial property terrorism insurance appears to be available nationwide at rates policyholders believe is reasonable, suggesting ample capacity.[11]

Note that this statement is very different from an assessment that such capacity would exist in the absence of a terrorism backstop. Again, it is important to emphasize that the majority of the coverage that exists in the market today exists because of the continued existence of the Terrorism Risk Insurance Program. Insurance broker Aon estimates that 70% to 80% of the market would encounter terrorism exclusions if the program were discontinued. Thus capacity in the market is largely contingent upon the continuation of the program. As detailed earlier in this testimony, policy language that would exclude coverage against terrorist attacks returned to the market each time the expiration of TRIA has loomed.

[10] *Market Conditions for Terrorism Risk Insurance 2010*, Report of the President's Working Group on Financial Markets.
[11] *Initial Results on Availability of Terrorism Insurance in Specific Geographic Markets*, GAO-08-919R, July 2008.

The so-called market for "standalone" terrorism coverage also provides evidence that in the absence of a Terrorism Risk Insurance Program, coverage capacity (supply) will fall well short of demand. Insurance brokers Marsh and Aon both report that the "theoretical" maximum amount of coverage available per risk in the "standalone" market is approximately $2 billion with larger sums available under some circumstances. This is in contrast with limits of just $150 million or less available in early 2002 before TRIA was enacted. At the time, such coverage also was subject to high deductibles equal to 7 to 10 percent of the stated value of the coverage.[12] While the sums available in the market today may seem large, especially in comparison to 2002, there are many risks for which the coverage is inadequate. Consider, for example, that back in 2001 (prior to the introduction of terrorism exclusions) the twin towers at the World Trade Center site were insured for $3.55 billion—more than what is generally available in the market today. Multibillion dollars risks are now quite common in the United States, from office and shopping complexes to large manufacturing facilities, sports stadiums, transportation hubs and energy infrastructure not to mention infrastructure such as bridges, tunnels and dams. These exposures exist in every state.

Reinsurance capacity, which was extremely limited in the aftermath of 9/11, is up as well. A 2011 report from reinsurance broker Guy Carpenter noted that there is between $6 billion and $8 billion of terrorism reinsurance capacity available in the U.S. market, but cautions that the market remains vulnerable to a major terrorism loss. The $6 billion to $8 billion in terrorism reinsurance capacity stands in stark contrast to approximately $100 billion in reinsurance capacity available in the market today against traditional risks (mostly property catastrophe risks). A continued cautious approach is clearly required. Indeed, many modeled terrorism loss scenarios result in insured losses in the tens or even hundreds of billions of dollars—some even exceeding the claims paying capital of the entire industry. As noted previously, much of the capacity in the market today is predicated on the existence of the Terrorism Risk Insurance Program. In the absence of the program, reinsurance capacity would be greatly reduced.

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[12] *September 11, 2001: One Hundred Minutes of Terror that Changed the Global Insurance Industry Forever*, Robert P. Hartwig, John Liner Review, January 2002.

Capital Markets and Terrorism Risk

Capital markets are playing an increasingly important role in providing capacity against losses arising from large natural disaster events which are becoming increasingly frequent in the United States and around the world. Capital market reinsurance capacity for U.S. natural catastrophe risks is estimated at $30 billion to $40 billion. However, investor appetite for catastrophe risk is so far limited to natural catastrophes such as hurricanes and earthquakes. Investors are attracted to investments in backing natural disasters risks in part because the performance of these assets is entirely uncorrelated with the performance of traditional financial market instruments such as stocks and bonds. A recession, for example, will impact the value of stocks and corporate bond prices but will have no impact on the likelihood of sustaining a loss on a catastrophe bond.

Investors to date have shown no appetite for terrorism risk because in the event of a major terrorist attack the performance of securitized terrorism risk instruments (such as catastrophe bonds) and tradition equity market and fixed income investment vehicles are likely to be *highly correlated.* For example, a large-scale terrorist attack could cause bonds exposed to the event to lose all or part of their value, leading to large losses for investors while stock markets plunge (as they did in the wake of the September 11, 2001 attack). Investor disinterest in terrorism risk is also a function of the inability to model and therefore price) such risks with anything close to the same degree of precision as tradition natural disaster risk.

Changes in the Terrorism Threat Landscape and Impacts on Terrorism Insurance Markets

In the immediate aftermath of 9/11 the ability of commercial policyholders to purchase adequate limits of terrorism coverage at affordable prices was severely constrained. Commercial property owners and businesses were faced with substantially reduced protection for terrorism-related risks, in addition to higher property/casualty rates overall. As a result, many were forced to go without coverage or only partly insure their assets.

Today, reports of property owners having problems securing terrorism coverage due to a lack of capacity in the market are no longer making headline news. Indeed, it is therefore tempting to conclude that in the eleven years since TRIA was first implemented that insurance markets have fully adjusted to the post-9/11 environment and that insurers and reinsurers have concluded that terrorism is a fully insurance risk.

The reality is quite different. The fact of the matter is that terrorism risk today is almost every bit as uninsurable as it was a decade ago. Recent major successes in the war on terror, including the killing of al-Qaida leader Osama bin Laden in 2011, do not alter this conclusion. This is because the current stability in the terrorism insurance market in the United States is due almost entirely to two factors:

(i) There has been no successful large scale terrorist attack on U.S. soil since 2001, and
(ii) TRIA remains in place.

The influence of both of these factors is discussed in the sections that follow.

Absence of Successful Attacks Does Not Imply Terrorism Risk is Inconsequential

The fact that there has been no successful terrorist attack in the United States in eleven years is a remarkable achievement. It is a testimony to the hard work and dedication of this nation's counterterrorism agencies and the bravery of the men and women in uniform who fought and continue to fight battles abroad to keep us safe here at home.

Unfortunately, the threat from terrorist attack in the United States is both real and substantial and will remain as such for the foreseeable future. Indeed, the U.S. State Department warned in a recent report that despite the death of bin Laden and other key al-Qaeda figures, the terrorist network's affiliates and adherents remain adaptable and resilient, and constitute "an enduring and serious threat to our national security."[13]

[13] *Country Reports on Terrorism 2011*, U.S. Department of State, July 31, 2012.

Table 2 below shows that interest in attacking targets within the United States remains undiminished—with four terrorist plots executed or interdicted within the past year alone. Indeed, it is clear from Table 2 that in addition to an ongoing threat from foreign terrorist networks, the United States also faces homegrown (domestic) terrorist threats from radical individuals, who may be inspired by al-Qaida and others, but may have little or no actual connection to militant groups.

Catastrophe modeler Risk Management Solutions (RMS) points to an increase in the number of homegrown plots in the U.S. in recent years.[14] Many of these have been thwarted, such as the 2012 attempt by Quazi Ahsam Nafis to blow up the Federal Reserve Bank of New York and Mohamed Osman Mohamud who targeted a Portland, Oregon, Christmas tree lighting ceremony. Also among the more notable unsuccessful attacks was an April 2013 attempt to blow up an Amtrak train en route between New York and Toronto. Other thwarted attacks against passenger and cargo aircraft, including the Christmas Day 2009 attempt to blow-up a jet over Detroit, are indicative of an ongoing risk to aviation infrastructure.

Table 2 also shows that terrorists are interesting in attacking targets across the United States, not just in large urban areas. Cities such as Springfield, Illinois and Lubbock, Texas, have also been targeted. It also important to note that the largest act of domestic terrorism in United States history was the truck bombing of the Alfred P. Murrah Federal Building in Oklahoma City in April 1995, which killed 166 people and produced insured property losses totaling $189 million (in 2012 dollars).

Another evolving threat is cyber-terrorism. Recent high profile attacks, such as the sabotaging of Iran's nuclear program via the Stuxnet computer worm and malicious infiltration attempts here in the U.S. by foreign entities, underscore the growing threat to both national security and the economy.

All these factors suggest that terrorism risk will be a constant and evolving threat for the foreseeable future.

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[14] RMS Terrorism Risk Briefing, July 2012.

Table 2

RECENT TERRORIST ATTACKS AND ATTEMPTS IN THE UNITED STATES

Date	Location	Event
April 15, 2013	Boston, MA	Brothers Tamerlan and Dzhokhar Tsarnaev detonate two pressure cooker bombs near the finish line of the Boston Marathon, killing 3 and injuring 264
April, 2013	New York City, NY-Toronto	Two suspects with al-Qaida links arrested in Toronto, Canada for alleged plot to blow up Amtrak passenger train en route from New York City to Toronto
November, 2012	New York City, NY	Brothers Raees Alam Qazi and Sheheryar Alam Qazi arrested and charged with conspiring to detonate a weapon of mass destruction targeting a New York City landmark
October, 2012	New York City, NY	Quazi Mohammad Rezwanul Ahsan Nafis arrested in plot to blow up Federal Reserve Bank in New York City
August, 2012	Ludowici, GA	Four U.S. soldiers charged in connection with murder and illegal gang activity, linked to foiled plot to commit domestic acts of terrorism, including overthrowing the government and assassinating the President
May, 2012	TBD	Foiled underwear bomb plot to bring down U.S.-bound commercial airliner around the anniversary of bin Laden's death
July 27, 2011	Fort Hood, TX	U.S. Army Pfc Naser Jason Abdo arrested and charged with plotting bomb attack on fellow soldiers at Fort Hood
June 22, 2011	Seattle, WA	Two men arrested in plot to attack military recruiting station in Seattle
May 11, 2011	New York City, NY	Ahmed Ferhani and Mohamed Mamdouh arrested in plot to attack Manhattan synagogue.
February 23, 2011	Lubbock, TX	Foiled plot to bomb military and political targets, including former President George W. Bush in New York, Colorado and California
December 8, 2010	Baltimore, MD	Attempted bombing of Armed Forces recruiting center by U.S. citizen Antonio Martinez, aka Muhammad Hussain
November 26, 2010	Portland, OR	Attempted bombing at Christmas tree lighting ceremony in downtown Portland by naturalized U.S. citizen Mohamed Osman Mohamud
October, 2010	Washington, D.C.	Attempted plot to bomb D.C.-area metro stations
May 1, 2010	New York City, NY	Attempted SUV bombing in Times Square, New York City, by naturalized U.S. citizen Faisal Shahzad
December 25, 2009	Over Detroit, MI	Attempted bombing of Northwest Airlines passenger jet over Detroit by underwear bomber Umar Farouk Abdulmutallab
September, 2009	New York City, NY	U.S. resident Najibullah Zazi and others charged with conspiracy to use weapons of mass destruction in New York City
September, 2009	Springfield, IL	Attempted plot to detonate a vehicle bomb at the federal building in Springfield.
September, 2009	Dallas, TX	Attempted bombing of skyscraper in Dallas
May, 2009	New York City, NY	Foiled plot to bomb Jewish synagogue and shoot down military planes in New York City
May, 2009	Various U.S. targets	Conviction of Liberty City six for conspiring to plan attacks on U.S. targets, including Sears Tower, Chicago

Source: Federal Bureau of Investigation (FBI); various news reports; Insurance Information Institute.

Potential Impacts If TRIA Is Not Extended

Without question, TRIA and its successors are the principal reason for the continued stability in the insurance and reinsurance market for terrorism insurance today. As discussed previously, TRIA is credited with restoring terrorism coverage in commercial insurance policies upon its enactment in late 2002.

Potential macroeconomic effects of allowing TRIA to expire—reduced economic growth and fewer jobs—were discussed earlier. In terms of impacts on insurance markets there is no question that coverage will become more expensive and less available—and in many cases unavailable. The question is not a theoretical one. In 2004, more than a year before the original Act's expiration at year-end 2005, terrorism exclusions once again emerged for policies with exposure extending into 2006. This was an unmistakable indication that insurance and reinsurance markets felt that terrorism risk, at least for larger scale attacks, remained uninsurable in the private sector. After Congress agreed to extend the program for another two years under the Terrorism Risk Insurance Extension Act of 2005 (TRIEA), terrorism coverage remained available and affordable in the market. However, with TRIEA's looming expiration in year-end 2006, terrorism exclusions once again appeared in the market, signaling the market's assessment that terrorism risk remained fundamentally uninsurable. These exclusions largely disappeared following passage of a 7-year extension of the program under the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA). With TRIPRA's expiration now a little more than one year away (year-end 2014), it is virtually certain that terrorism exclusions will soon reappear in the market. Indeed, insurance broker Aon estimates that at least 80 percent of the commercial property market will be impacted by these exclusions and other restrictions.

Studies by various organizations, including the University of Pennsylvania's Wharton School Risk Center, the RAND Corporation and the Organization for Economic Co-operation and Development (OECD), have supported the idea of a substantive federal role in terrorism insurance. In particular, the Wharton School found that TRIA has had a positive effect on availability of terrorism coverage and also has significantly contributed to reducing insurance premiums.[15] The OECD notes, however, that the financial (capital) markets have thus far shown little appetite for terrorism risk.

Evidence from Other Countries: Terrorism Risk Insurance Programs Abroad

Additional evidence that terrorism risk is fundamentally uninsurable comes from abroad. A number of countries have established their own terrorism risk insurance programs and these have operated successfully, often for many years. Australia, Austria, Belgium, France, Germany, the Netherlands, Spain, Switzerland and the United Kingdom have all created programs to cover terrorism in the event of an attack on their own soil.[16] None of these countries is considering the discontinuation of its program.

This begs the question as to why—twelve years after the 9/11 attack and a decade after the initial terrorism risk insurance program legislation was enacted—terrorism risk, particularly for large-scale attacks, is still viewed as uninsurable? The answer is surprisingly simple and explains why even the absence of a successful major attack on U.S. soil since 2001 does not alter this assessment.

Obstacles to Insuring Losses Arising from Acts of Terrorism

Simply put, acts of terror violate all four of the basic requirements traditionally associated with insurability of a risk. In situations where these requirements cannot be met, it is difficult or impossible to ascertain the premium to be charged and/or difficult or impossible to achieve the necessary spread of risk to avoid excessive exposure to catastrophic loss, thereby threatening the insurer's solvency. Consequently, such a risk would generally be deemed to be commercially *not* viable (i.e., insurable) in whole or in part.

[15] *Evaluating the Effectiveness of Terrorism Risk Financing Solutions*, Howard C. Kunreuther and Erwann O. Michel-Kerjan, September 2007, National Bureau of Economic Research.

[16] In 1993, the British government formed a mutual reinsurance pool for terrorist coverage following acts of terrorism by the Irish Republican Army. Insurance companies pay premiums at rates set by the pool. The primary insurer pays the entire claim for terrorist damage but is reimbursed by the pool for losses in excess of a certain amount per event and per year based on its share of the total market. Following 9/11, coverage was extended to cover all risks, except war, including nuclear and biological contamination, aircraft impact and flooding, if caused by terrorist attacks. The British government acts as the reinsurer of last resort, guaranteeing payments above the industry retention.

The four basic requirements for insurability of a risk are detailed below (as well in Exhibits 4A and 4B), with a description of how terrorism risk violates each requirement:

1. **Estimable Frequency:** Insurers require a large number of observations to develop predictive, statistically sound rate-making models (an actuarial concept known as "credibility"). For example, insurers handle millions of auto, home, workers compensation and business property claims every year, providing them with vast amounts of data from which they can reliably estimate the frequency of such claims. For major catastrophic risks such as hurricanes and earthquakes that occur less frequently insurers still maintain databases with hundreds or even thousands of these events, supplemented by sophisticated catastrophe models, that help provide statistically reliable estimates of frequency. Terrorism risk is clearly different in this respect.

   Obstacle: There are very few data points on which to base frequency estimates for acts of terror in the United States, thus estimates lack any true actuarial credibility. The opinions of experts on the likelihood of terrorist attacks, which might be viewed by some as substitutes for actuarially credible data, are also highly subjective. At any given time, there is a wide range of viewpoints among national security experts on the likelihood, location and/or attack modality. Moreover, insurers have no access to data used internally by counterterrorism agencies. Given the paucity of historical data and diversity and shifting nature of expert opinions, catastrophe models used to estimate terrorism risk are relatively undeveloped compared to those used to assess natural hazard risks. The bottom line is that estimating the frequency of terror attacks with any degree of accuracy (credibility) is extraordinarily challenging, if not impossible in many circumstances.

2. **Estimable Severity:** Insurability requires that the maximum possible/probable loss be estimable in order to calculate the insurer's exposure (in dollar terms) and minimize its "probability of ruin." No insurer can expose itself to losses of a magnitude that present an unreasonable risk of insolvency.

Obstacle: Potential losses arising from terrorist attacks are virtually unbounded. In this sense terrorism risk is akin to war risk, which is almost universally excluded from commercial insurance policies worldwide. Consequently, losses arising from acts of terror can easily exceed an insurer's claims paying capital resources. Workers compensation coverage, which does not permit any exclusions or limitation if injuries or deaths arise from terrorist acts, can lead to extreme losses that on their own could potentially bankrupt an insurer under some attack scenarios. In addition, when it comes to estimating losses from potential terrorist attacks there also appears to be significant variability in outcomes (i.e., disagreement on estimated severity impacts), underscoring the degree of uncertainty associated with potential terrorist attacks.

3. **Diversifiable Risk:** Insurability requires that the losses can be spread across a large number of risks. This is an application of the "Law of Large Numbers" and helps makes losses more manageable and less volatile. Failure to achieve an adequate spread of risk increases the risk of insolvency in the same way that an undiversified portfolio of stocks (or any asset) is riskier than a well-diversified portfolio.

   Obstacle: Terrorism attacks are likely to be highly concentrated geographically (e.g., World Trade Center site), concentrated within an industry (e.g., power plants, airports) or within a certain span of time (e.g., coordinated attack).

4. **Random Loss Distribution/Fortuity:** Insurability requires that the probability of a loss occurring be random or fortuitous. This implies that individual events must be unpredictable in terms of timing, location and magnitude.

Obstacle: Terrorism attacks are planned, coordinated and deliberate acts of destruction. Again, they are likely to be highly concentrated geographically (e.g., World Trade Center site) or concentrated within an industry (e.g., power plants). Terrorists engage in "dynamic target shifting" whereby terrorists shift from "hardened targets" to "soft targets" which implies that losses are not random or fortuitous in nature. The April 2013 Boston Marathon bombing was an example of an attack on a soft target. It is also not difficult to imagine attacks occurring in the United States similar to the September 2013 attack on an upscale shopping mall (another soft target) in Nairobi, Kenya, by al-Shabaab, a Somali-based terrorist group with links to al-Qaeda.

Additional Issues for Consideration in Conjunction with TRIA Reauthorization

Certification Deadline: While TRIA spells out a highly detailed set of criteria that must be met for an event to be officially certified as a "terrorist act," TRIA offers no timeline or deadline by which such a certification must be made. Although the Boston Marathon bombings occurred more than five months ago (on April 15, 2013), there has to date been no certification by the Treasury Department nor has there been any statement by Treasury that the event would not be certified. Indeed, Treasury has offered no guidance as to whether any such determination is ever forthcoming. This situation has created some uncertainty and confusion for policyholders, insurers and other impacted parties. A simple and reasonable solution would be to require that a certification determination must be made within a specified number of days after the event.

Cyber Terrorism: The threat both to national security and the economy posed by cyber terrorism is a growing concern for governments and businesses around the world, with critical infrastructure, such as power plants, transportation, and communication infrastructure at risk.[17] The Department of Homeland Security received reports of some 198 attacks on critical infrastructure systems in the U.S. in 2012, a 52 percent increase on 2011.[18]

Former U.S. Homeland Security Secretary Janet Napolitano recently warned that a "cyber 9/11" could happen imminently and noted that critical infrastructure – including water, electricity and gas – is very vulnerable to such a strike.[19]

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[17] *Cyber Risks: The Growing Threat*, Robert P. Hartwig and Claire Wilkinson, Insurance Information Institute, April 2013.
[18] *As Hacking Against U.S. Rises, Experts Try to Pin Down Motive*, the New York Times, March 3, 2013
[19] *Napolitano warns of risk of major cyber attack*, Newsday, January 24, 2013.

Earlier, in an October 2012 speech then U.S. Defense Secretary Leon Panetta warned that the United States was facing a possible "cyber Pearl Harbor" scenario, and increasingly vulnerable to foreign cyber attacks on its critical infrastructure networks. Such attacks are targeting the computer control systems that operate chemical, electricity and water plants and transportation networks, Panetta said.

Summary

In the twelve years since the tragedy of the September 11, 2001 terrorist attack on the United States, much has been learned about the nature of terrorism risk and its insurability. There is no question that the Terrorism Risk Insurance Act and its successors brought much needed stability to the market in the aftermath of the most costly insurance loss in global history. In the decade since, private sector insurers, reinsurers and the federal government have successfully partnered with one another in order to maintain that stability, providing tangible benefits for businesses large and small—and their employees—all across America.

The looming expiration of the TRIA at the end of 2014 brings to a head the question of whether terrorism risk is now, or ever will be, a risk that can be managed entirely within the private sector. The evidence, both in the United States and from similar programs abroad, is that market stability in terms of both pricing and availability of terrorism coverage, as well as the ability to maintain adequate and expanding levels of capacity over time, are contingent on the continued existence of the Terrorism Risk Insurance Program.

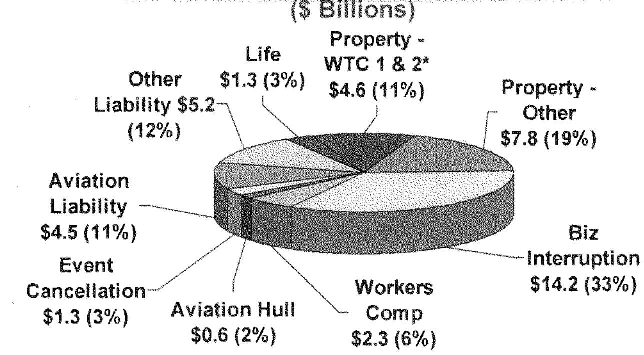
Thank you for you for the opportunity to testify before the Committee today. I would be happy to respond to any questions you may have.

Exhibit 1

Loss Distribution by Type of Insurance from Sept. 11 Terrorist Attack ($ 2012)

INSURANCE INFORMATION INSTITUTE

($ Billions)



Total Insured Losses Estimate: $42.1B

*Loss total does not include March 2010 New York City settlement of up to $657.5 million to compensate approximately 10,000 Ground Zero workers or any subsequent settlements.

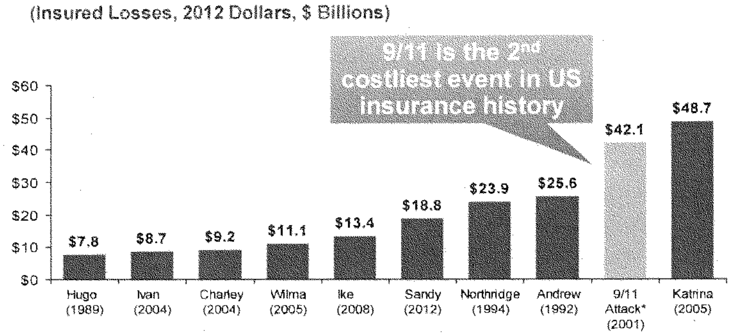
Source: Insurance Information Institute.

Exhibit 2

Top 10 Most Costly Disasters in U.S. History

INSURANCE INFORMATION INSTITUTE

(Insured Losses, 2012 Dollars, $ Billions)



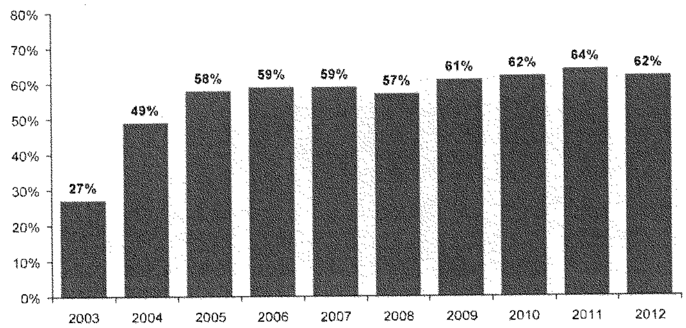
* Insured loss estimate for Sep. 11 terrorist attack includes property, business interruption, workers comp, aviation hull, liability, event cancellation and life insurance losses.

Sources: PCS; Insurance Information Institute inflation adjustments to 2012 dollars using the CPI. 11

Exhibit 3

Terrorism Insurance Take-up Rates, By Year, 2003-2012

INSURANCE INFORMATION INSTITUTE



In 2003, the first year TRIA was in effect, the terrorism take-up rate was 27 percent. Since then, it has increased steadily, remaining in the low 60 percent range since 2009.

Source: Marsh Global Analytics, *2013 Terrorism Risk Insurance Report*, May 2013.

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Exhibit 3

Pyramid of Taxpayer Protection: Strong, Stable, Sound and Secure

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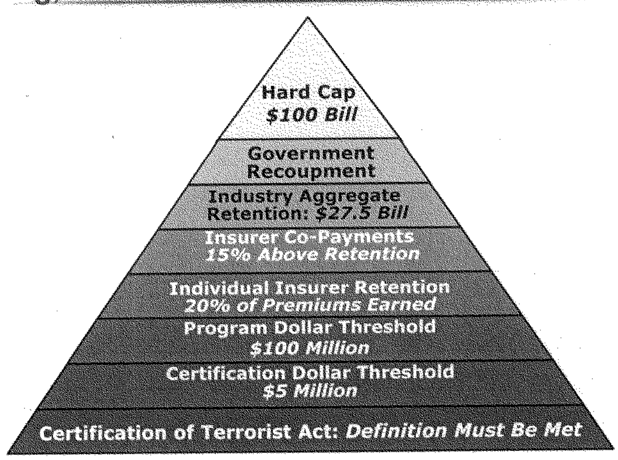

Exhibit 4A

Terrorism Violates Traditional Requirements for Insurability

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Requirement	Definition	Violation
Estimable Frequency	•Insurance requires large number of observations to develop predictive rate-making models (an actuarial concept known as credibility)	•Very few data points •Terror modeling still in infancy, untested. •Inconsistent assessment of threat
Estimable Severity	•Maximum possible/ probable loss must be at least estimable in order to minimize "risk of ruin" (insurer cannot run an unreasonable risk of insolvency though assumption of the risk)	•Potential loss is virtually unbounded. •Losses can easily exceed insurer capital resources for paying claims. •Extreme risk in workers compensation and statute forbids exclusions.

Source: Insurance Information Institute

Exhibit 4B

Terrorism Violates Traditional Requirements for Insurability (cont'd)

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Requirement	Definition	Violation
Diversifiable Risk	•Must be able to spread/distribute risk across large number of risks •"Law of Large Numbers" helps makes losses manageable and less volatile	•Losses likely highly concentrated geographically or by industry (e.g., WTC, power plants)
Random Loss Distribution/ Fortuity	•Probability of loss occurring must be purely random and fortuitous •Events are individually unpredictable in terms of time, location and magnitude	•Terrorism attacks are planned, coordinated and deliberate acts of destruction •Dynamic target shifting from "hardened targets" to "soft targets" •Terrorist adjust tactics to circumvent new security measures •Actions of US and foreign govts. may affect likelihood, nature and timing of attack

Source: Insurance Information Institute

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TERRORISM RISK: A CONSTANT THREAT

Impacts for Property/Casualty Insurers

JUNE 2013

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INTRODUCTION

The April 15, 2013 bombing near the finish line at the Boston Marathon marked the first successful terrorist attack on U.S. soil in more than a decade. The attack left three dead and 264 injured.

Three days after the bombing, the suspects—brothers Dzhokhar and Tamerlan Tsarnaev—took to the streets, killing a police officer, carjacking a vehicle, and engaging in a shootout with police in the Boston suburb of Watertown, which left another police officer injured and ultimately left Tamerlan Tsarnaev dead. Suspect Dzhokhar Tsarnaev escaped, but was eventually found hiding in Watertown where he was arrested on the evening of April 19, after an unprecedented manhunt and shutdown of a major city, during which millions of residents had to remain indoors and Boston's entire public transportation system and most businesses were shuttered.

Dzhokhar was charged on April 22 with using and conspiring to use a weapon of mass destruction resulting in death and with malicious destruction of property resulting in death. The ongoing investigation is heing led by the Federal Bureau of Investigation (FBI). However, among the facts to emerge so far are that the Tsaruaev brothers planned additional attacks, specifically in New York City's Times Square.

The Boston Marathon attack—twin explosions of pressure cooker bombs occurring within 12 seconds of each other in the Back Bay downtown area—adds to a growing list of international terrorism incidents that have occurred since the terrorist attack of September 11, 2001.

The 2002 Bali bombings, the 2004 Russian aircraft and Madrid train bombings, the London transportation bombings of 2005 and the Mumbai attacks of 2008 all had a profound influence on the 2001 to 2010 decade. Then came 2011, a landmark year, which simultaneously saw the death of al-Qaida fouuder Osama bin Laden and the 10-year anniversary of September 11.

While the loss of biu Laden and other key al-Qaida figures put the network on a path of decline that is difficult to reverse, the State Department warned that al-Qaida, its affiliates and adherents remained adaptable and resilient, and constitute "an enduring and serious threat to our national security."

The Boston bombing serves as an important reminder that countries also face homegrown terrorist threats from radical individuals who may be inspired by al-Qaida and others, but may have little or no actual connection to militant groups.

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In a recent press release, catastrophe modeler RMS assesses that the U.S. terrorist threat will increasingly come predominantly from such homegrown extremists, who due to the highly decentralized structure of such "groups" are difficult to identify and apprehend.[1]

Until the Boston bombing, many of these potential attacks had been thwarted, such as the 2010 attempted car bomb attack in New York City's Times Square and the attempt by Najibullah Zazi to bomb the New York subway system ***(Figure 1)***. Other thwarted attacks against passenger and cargo aircraft indicate the ongoing risk to aviation infrastructure.

Figure 1
RECENTLY THWARTED TERRORIST ATTACK ATTEMPTS IN THE U.S.

Date	Location	Event
April, 2013	New York City, NY-Toronto	Two suspects with al-Qaida links arrested in Toronto, Canada for alleged plot to blow up Amtrak passenger train en route from New York City to Toronto
November, 2012	New York City, NY	Brothers Raees Alam Qazi and Sheheryar Alam Qazi arrested and charged with conspiring to detonate a weapon of mass destruction targeting a New York City landmark
October, 2012	New York City, NY	Quazi Mohammad Rezwanul Ahsan Nafis arrested in plot to blow up Federal Reserve Bank in New York City
August, 2012	Ludowici, GA	Four U.S. soldiers charged in connection with murder and illegal gang activity, linked to foiled plot to commit domestic acts of terrorism, including overthrowing the government and assassinating the President
May, 2012	TBD	Foiled underwear bomb plot to bring down U.S.-bound commercial airliner around the anniversary of bin Laden's death
July 27, 2011	Fort Hood, TX	U.S. Army Pfc Naser Jason Abdo arrested and charged with plotting bomb attack on fellow soldiers at Fort Hood
June 22, 2011	Seattle, WA	Two men arrested in plot to attack military recruiting station in Seattle
May 11, 2011	New York City, NY	Ahmed Ferhani and Mohamed Mamdouh arrested in plot to attack Manhattan synagogue
February 23, 2011	Lubbock, TX	Foiled plot to bomb military and political targets, including former President George W. Bush in New York, Colorado and California
December 8, 2010	Baltimore, MD	Attempted bombing of Armed Forces recruiting center by U.S. citizen Antonio Martinez, aka Muhammad Hussain
November 26, 2010	Portland, OR	Attempted bombing at Christmas tree lighting ceremony in downtown Portland by naturalized U.S. citizen Mohamed Osman Mohamud
October, 2010	Washington, D.C.	Attempted plot to bomb D.C.-area metro stations
May 1, 2010	New York City, NY	Attempted SUV bombing in Times Square, New York City, by naturalized U.S. citizen Faisal Shahzad
December 25, 2009	Over Detroit, MI	Attempted bombing of Northwest Airlines passenger jet over Detroit by underwear bomber Umar Farouk Abdulmutallab

[1] Bombings at the Boston Marathon Raise Specter of Homegrown Terrorism, RMS press release, April 24, 2013.

Date	Location	Event
September, 2009	New York City, NY	U.S. resident Najibullah Zazi and others charged with conspiracy to use weapons of mass destruction in New York City
September, 2009	Springfield, IL	Attempted plot to detonate a vehicle bomb at the federal building in Springfield
September, 2009	Dallas, TX	Attempted bombing of skyscraper in Dallas
May, 2009	New York City, NY	Foiled plot to bomb Jewish synagogue and shoot down military planes in New York City
May, 2009	Various U.S. targets	Conviction of Liberty City six for conspiring to plan attacks on U.S. targets, including Sears Tower, Chicago

Source: Federal Bureau of Investigation (FBI); various news reports; Insurance Information Institute.

A 2012 report from the U.S. Department of State highlighted the changing nature of the global terrorism threat, noting that the total number of worldwide terrorist attacks in 2011 was more than 10,000 in 70 countries, resulting in more than 12,500 deaths.[2] While large, that figure represents a drop of 12 percent from 2010. More than 75 percent of the world's attacks occurred in South Asia and the Near East, and 85 percent of attacks in these regions occurred in just three countries: Afghanistan, Iraq and Pakistan.

Counterterrorism success in 2011 came as a number of countries across the Middle East and North Africa saw political demonstrations and social unrest. The movement known as the Arab Spring was triggered initially by an uprising in Tunisia that began back in December 2010. Unrest and instability in this region continues in 2013.

Meanwhile, the July 2011 attack by a lone right-wing extremist in Norway—a country rarely targeted in the past—that left more than 70 people dead and dozens injured, underscores the inability of any country to escape from terrorism, the State Department notes.

Another evolving threat is cyberterrorism. The threat both to national security and the economy posed by cyberterrorism is a growing concern for governments and businesses around the world, with critical infrastructure, such as nuclear power plants, transportation and utilities, at risk.

All these factors suggest that terrorism risk will be a constant, evolving and potentially expanding threat for the foreseeable future.

The looming expiration at the end of 2014 of the government-backed Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) is also prompting

[2] Country Reports on Terrorism 2011, U.S. Department of State, July 31, 2012.

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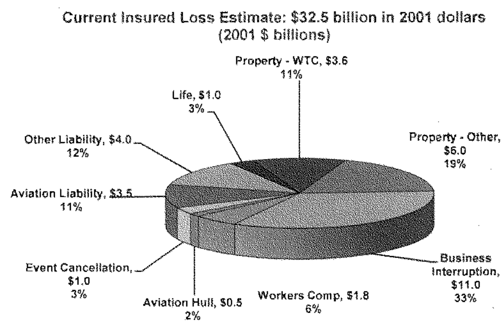
increased dialogue between industry and government about terrorism risk, a discussion that has gained critical importance in tbe wake of the Boston bombing.

THE IMPACT OF 9/11 ON INSURERS

For property/casualty insurers and reinsurers, the impact of the terrorist attack of September 11, 2001, was substantial, producing insured losses of about $32.5 billion, or $42.1 billion in 2012 dollars. Losses were paid out across many different lines of insurance, including property, business interruption, aviation, workers compensation, life and liability ***(Figures 2 and 3)***. The loss total does not include the March 2010 settlement of up to $657.5 million anuounced by New York City officials and plaintiffs' lawyers to compensate about 10,000 workers whose health was damaged during the rescue and cleanup at the World Trade Center, or any subsequent settlements (see later section: Gronnd Zero Workers and Health Claims).

Figure 2
SEPTEMBER 11 INDUSTRY LOSS ESTIMATES*



*Loss total does not include NYC March 2010 settlement of up to $657.5 million to compensate about 10,000 Ground Zero workers.

Source: Insurance Information Institute.

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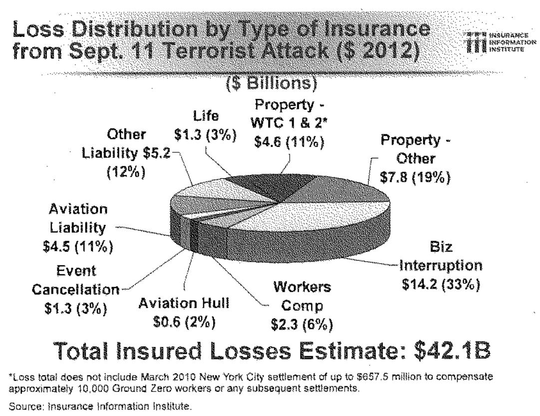
Figure 3



A total of 2,976 people lost their lives in the September 11, 2001 terrorist attacks in New York, Washington, D.C., and Pennsylvania, excluding the 19 hijackers. It remains the worst terrorist attack on record in terms of fatalities and insured property losses, which totaled about $24.6 billion (in 2012 dollars) ***(Figure 4)***. In the more than 10 years since 9/11 insurers have paid out many billions of dollars for other catastrophes, but until Hurricane Katrina in 2005 when insurers paid claims totaling more than $40 billion, 9/11 was the largest loss in the global history of insurance. By way of reference, superstorm Sandy, which impacted the Northeast United States including the New York metropolitan area, produced $18.6 billion in private insured losses.

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Figure 4
WORST TERRORIST ACTS, INSURED PROPERTY LOSSES*
(2012 $ millions)

Rank	Date	Country	Location	Event	Insured property loss (1)	Fatalities
1	September 11, 2001	United States	New York, Washington DC, Pennsylvania	Hijacked airliners crash into World Trade Center and Pentagon	$24,364	2,982
2	April 24, 1993	United Kingdom	London	Bomb explodes near NatWest tower in the financial district	$1,176	1
3	June 15, 1996	United Kingdom	Manchester	Irish Republican Army (IRA) car bomb explodes near shopping mall	$966	0
4	April 10, 1992	United Kingdom	London	Bomb explodes in financial district	$870	3
5	February 26, 1993	United States	New York	Bomb explodes in garage of World Trade Center	$810	6
6	July 24, 2001	Sri Lanka	Colombo	Rebels destroy 3 airliners, 8 military aircraft and heavily damage 3 civilian aircraft	$517	20
7	February 9, 1996	United Kingdom	London	IRA bomb explodes in South Key Docklands	$336	2
8	June 23, 1985	North Atlantic	Irish Sea	Bomb explodes on board of an Air India Boeing 747	$209	329
9	April 19, 1995	United States	OK, Oklahoma City	Truck bomb crashes into government building	$189	166
10	September 12, 1970	Jordan	Zerqa, Dawson's Field (disused RAF airstrip in desert)	Hijacked Swissair DC-8, TWA Boeing 707, BOAC VC-10 dynamited on ground	$165	0
11	September 6, 1970	Egypt	Cairo	Hijacked PanAm B-747 dynamited on ground	$143	0
12	April 11, 1992	United Kingdom	London	Bomb explodes in financial district	$125	0
13	November 26, 2008	India	Mumbai	Attack on two hotels; Jewish center	$109	172
14	March 27, 1993	Germany	Weiterstadt	Bomb attack on a newly built, still unoccupied prison	$92	0
15	December 30, 2006	Spain	Madrid	Bomb explodes in car garage at Barajas Airport	$75	2
16	December 21, 1988	United Kingdom	Lockerbie	Bomb explodes on board of a PanAm Boeing 747	$73	270
17	July 25, 1983	Sri Lanka		Riot	$61	0
18	July 7, 2005	United Kingdom	London	Four bombs explode during rush hour in a tube and bus	$61	52
19	November 23, 1996	Comoros	Indian Ocean	Hijacked Ethiopian Airlines Boeing 767-260 ditched at sea	$59	127
20	March 17, 1992	Argentina	Buenos Aires	Bomb attack on Israel's embassy in Buenos Aires	$49	24

(1) Includes bodily injury and aviation hull losses. Updated to 2012 dollars by the Insurance Information Institute using the U.S. Bureau of Labor Statistics' CPI Inflation Calculator.
*Insured losses for the April 15, 2013 Boston Marathon bombings had yet to be determined, as of May 31, 2013.

Source: Swiss Re.

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As construction progresses on one World Trade Center (a.k.a. Freedom Tower) insurance claims dollars continue to play an essential and highly visible role in rebuilding lower Manhattan. The many billions of dollars in insurance payouts have also mitigated the overall economic impact of the 9/11 attack—estimated initially by the Milken Institute as approaching $200 billion overall.

Before 9/11 terrorism exclusions were virtually nonexistent in commercial insurance contracts sold in the United States. Following the attack, insurers moved to exclude coverage. Only when the Terrorism Risk Insurance Act (TRIA) was enacted by Congress in November 2002 did coverage for terrorist attacks resume. TRIA established a public/private risk-sharing partnership that allows the federal government and the insurance industry to share losses in tbe event of a major terrorist attack. The program is designed to ensure that adequate resources are available for businesses to recover and rebuild if they become the victims of a terrorist attack.

Since its initial enactment in 2002 the terrorism risk insurance program has been revised and extended twice. The most recent extension—the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA)—ensures its continuation until December 31, 2014. However, the portion of the loss insurers would pay in the event of a terrorist attack has increased significantly over the years. Insurers are also solely responsible for terrorism losses that impact non-TRIA lines, such as private passenger auto and homeowners insurance and group life. Less than half of the property/casnalty insurance premiums are written in lines of insurance backstopped by TRIPRA.[3]

By all accounts the terrorism risk insurance program is an unqualified success—a rarity among federal programs—that has achieved all its goals.[4] The program not only succeeded in restoring stability to the country's vital insurance and reinsurance markets in the wake of the unprecedented market dislocations associated with September 11, 2001, terrorist attack, but it continues to deliver substantive, direct benefits to businesses, workers, consumers and the economy overall—all at little or no cost to taxpayers.

More recently, provisions of the terrorism risk insurance program have again come under attack. For example, the Obama administration's 2011 budget plan included

[3] For additional information go to www.marketstance.com. Questions can be emailed to info@marketstance.com or call (888) 777-2587.
[4] TRIA at Ten Years: The Future of the Terrorism Risk Insurance Program, Testimony of Robert P. Hartwig, Insurance Information Institute (I.I.I.) before the House Financial Services Subcommittee on Insurance, Housing, and Community Opportunity, September 11, 2012.

a proposal seeking to scale back federal support for the program, though the administration's latest 2014 budget proposal did not include a cut for the program.

FUTURE OF TRIPRA AND INSURANCE IMPLICATIONS

The government-backed Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) is set to expire at the end of 2014. The program's imminent expiration is prompting increased dialogue between industry and government, a discussion that has gained critical importance in the wake of the Boston bombing.

A February 2013 report for Congress by the Congressional Research Service (CRS) noted that since TRIA's passage, the private industry's willingness and ability to cover terrorism risk have increased.[5] Prices for terrorism coverage have generally trended downward, and some 60 percent of commercial policyholders have purchased coverage over the past few years. However, since this relative market calm has been under the umbrella of TRIA coverage, CRS said it was unclear how the insurance market would react to the expiration of the federal program.

Reinsurance broker Guy Carpenter notes that should TRIPRA not be extended, it wonld expect terrorism insurance to be greatly reduced in areas of the United States that have the most need for coverage, such as central business districts and other high risk areas.[6] Even in workers compensation, where terrorism insurance is mandated whether or not the backstop is available, Guy Carpenter says it would expect insurers to severely cnrtail their writings of risks in areas that have the highest risk, and therefore the greatest need for coverage.

Meanwhile, pricing for terrorism insurance could increase dramatically in a number of metropolitan areas and for numerous venues around the U.S. As a result, without the TRIPRA backstop, policyholder needs with regards to terrorism insurance would not be met and many would be left to self-insure the entire risk or portions of the risk, according to Guy Carpenter, meaning that any future terrorist acts could have a negative impact on U.S. economic activity. Ultimately, any dramatic change in TRIPRA could lead to contraction in the marketplace in both insurance and reinsurance, it concluded. It is critical to note, however, that in the absence of the TRIPRA, backstop infrastructure, commercial buildings, shopping malls and sporting venues outside of urhan areas are also vulnerable.

[5] Terrorism Risk Insurance: Issue Analysis and Overview of Current Program, Congressional Research Service (CRS), February 26, 2013.
[6] Tensions Building: The Changing Nature of Terrorism Risk and Coverage, Guy Carpenter, December 2012, and Future of TRIPRA and Implications on the (Re)Insurance Market, GCCapitalIdeas.com, December 24, 2012.

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Ratings agency A.M. Best has warned that in the event TRIPRA is not extended, insurer ratings could potentially suffer.[7] Specifically, A.M. Best said insurers that currently would be materially affected by the absence of TRIPRA and that cannot provide a sufficient action plan to reduce exposures to terrorism risks, likely will face rating pressure as the expiration date approaches. Initially, this pressure may result in the assignment of a negative outlook during the latter part of 2013.

Similarly, ratings agency Fitch has said failure by Congress to extend the Terrorism Risk Insurance Act could induce commercial insurers to retreat from larger metropolitan areas, reducing availability of terrorism insurance and potentially raising premium rates.[8] "Insurers' sophistication regarding terrorism risk has evolved significantly since 2001, with a heightened focus on managing risk aggregations in larger metropolitan areas. Still, the industry remains in a challenging position in terms of modeling and underwriting terrorism-related risk," Fitch said.

In its 2010 report on terrorism risk insurance market conditions, the President's Working Group on Financial Markets noted that the program provides incentive to property/casualty insurers and reinsurers who might not otherwise provide terrorism insurance at current capacity levels or prices.[9] A 2009 report by insurance broker Aon estimated that some 70 percent to 80 percent of the commercial property insurance market would revert to absolute exclusions for terrorism if TRIA is changed.[10]

HOW INSURERS TREAT TERRORISM RISK TODAY

In the immediate aftermath of 9/11 the ability of commercial policyholders to purchase adequate limits of terrorism coverage at affordable prices was severely constrained. Commercial property owners and businesses were faced with substantially reduced protection for terrorism related risks, in addition to higher property/casualty rates overall. The situation was particularly acute for owners of high profile "trophy" buildings located in major metropolitan areas. As a result, many were forced to go without coverage or only partly insure their assets.

Prior to the Boston Marathon bombing, reports of property owners, retail outlets or sporting events having problems securing terrorism coverage due to a lack of capacity in the market were no longer making headline news. It remains to be seen

[7] As Expiration of TRIPRA Approaches, Rating Pressure Increases, Best's Briefing, April 1, 2013.
[8] Higher Premiums if Terror Insurance Act Not Renewed, Fitch Wire, Fitch Ratings, May 6, 2013.
[9] *Market Conditions for Terrorism Risk Insurance 2010*, Report of the President's Working Group on Financial Markets.
[10] *Terrorism Update and Key Metrics Report* – May 2009, Aon Risk Services.

how the terrorism insurance market will react to this latest event, but catastrophe modeler RMS has said that the insurance of sports events is likely to be impacted.[11]

In general, insurance capacity may be more limited in certain high-risk cities for terrorism. A 2010 report on terrorism risk insurance market conditions by the President's Working Group on Financial Markets noted that while the availability and affordability of terrorism risk insurance provided by private insurers has improved since 2006, insurance capacity remains constrained for certain high-risk locations and properties. Some commercial insurance policyholders in high-risk urban areas also have difficulty in obtaining coverage at sufficient limits, it said.

The PWG analysis followed a July 2008 report from the U.S. Government Accountability Office (GAO) on the availability and affordability of terrorism coverage in large metropolitan areas.[12] It found that while commercial property terrorism insurance appears to be available nationwide at rates policyholders believe is reasonable, certain types of policyholders may have more difficulty obtaining the coverage amounts they need at prices they view as acceptable. These policyholders are typically owners of high-value properties in urban areas such as Manhattan where there is a high concentration of large buildings that are seen as potential terrorism targets.

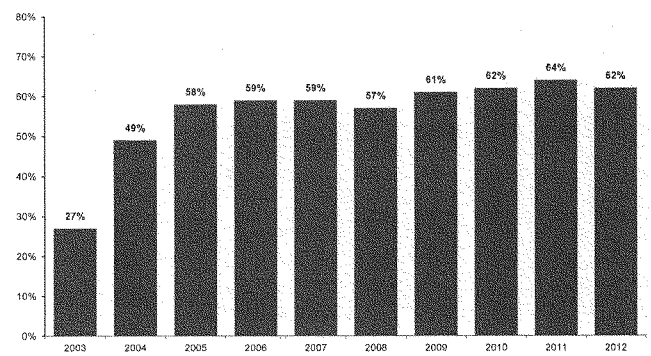
A 2012 report from reinsurance broker Guy Carpenter noted that unrest around the world, including the Arab Spring protests, as well as widespread protests in Europe and other regions, had begun to impact the terrorism (re)insurance market, not only in terms of supply and demand, but also in terms of how risks and coverages are defined.[13] Although it described capacity in the market as abundant, Guy Carpenter noted that civil unrest and/or riot coverages in some international terrorism programs were impacting several reinsurance carriers. The dramatic increase in global unrest had caused an increased frequency of localized or territory-specific losses in the facultative reinsurance market, Guy Carpenter said. As this report went to press, the impact of the Boston Marathon bombing on the market is still to be determined.

Industry data shows that the proportion of businesses buying property terrorism insurance (the take-up rate for terrorism coverage) has generally increased since the enactment of TRIA in 2002, as businesses across the United States had the opportunity to purchase terrorism coverage, usually at a reasonable cost. Take-up rates for workers compensation terrorism coverage are effectively 100 percent as this is a compulsory line of insurance for all businesses.

[11] Boston Marathon Bombing: Running Fear, RMS press release, April 17, 2013.
[12] Initial Results on Availability of Terrorism Insurance in Specific Geographic Markets, GAO-08-919R, July 2008.
[13] Tensions Building: The Changing Nature of Terrorism Risk and Coverage, Guy Carpenter, December 2012.

A May 2013 report from insurance broker Marsh found that the demand for terrorism insurance remains and the existence of TRIA plays a major role in the availability and affordability of coverage.[14] The percentage of companies buying property terrorism insurance—the terrorism take-up rate—has remained fairly constant since 2005. In 2003, the first full year TRIA was in effect, the take-up rate was 27 percent, but has since increased steadily, remaining in the low 60 percent range since 2009 ***(Figure 5)***.

Figure 5
TERRORISM INSURANCE TAKE-UP RATES BY YEAR



Source: Marsh Global Analytics

The companies surveyed by Marsh that bought terrorism coverage came from every industry sector. Of the 17 segments surveyed, media companies were most likely to include terrorism coverage as part of their property insurance in 2012, with the highest take-up rate, 81 percent, of any industry segment. Companies in the health care, financial, education and public entity sectors also had high take-up rates of above 70 percent, Marsh said.

Property terrorism insurance rates typically decrease as the size of the company increases, Marsh noted. Since 2010, companies with total insured value (TIV) less than $100 million experienced moderate median rate decreases, from $54 per

[14] *Marsh Market Update: 2013 Terrorism Risk Insurance Report,* May 2013.

million in 2010 to $49 per million in 2012. However, their terrorism premium rates remained significantly higher than those of larger companies.

Median rates for the largest companies stood at $19 per million in 2012. According to Marsh, this is generally in keeping with overall insurance pricing patterns. Larger companies typically purchase more insurance, which leads to lower rates compared to those for smaller companies.

A stand-alone market for terrorism insurance coverage also exists. The stand-alone market is an important alternative and/or supplement to TRIA coverage for some companies.

In its May 2013 report, Marsh noted that demand for terrorism and political violence insurance coverage has grown in the Middle East, Asia and North Africa following the so-called Arab Spring.

The stand-alone property terrorism insurance market offers coverage for both TRIA-certified and noncertified risks and enables companies to tailor capacity to their coverage needs. The primary industry segments purchasing stand-alone policies were the hospitality sector, large real estate firms and financial institutions. Lesser, but still significant, amounts were purchased in the retail, media, transportation, public entity and utilities segments.

Capacity in the stand-alone terrorism insurance market has increased considerably for exposures outside central business districts, according to Marsh.

Marsh estimates approximately $750 million to $2 billion per risk in stand-alone capacity is available to companies that do not have sizeable exposures in locations where insurers have aggregation problems. Capacity excess of $2 billion is available but more costly.

For locations where stand-alone insurers have aggregation issues, the estimated market capacity is approximately $850 million or lower in some cases. Additional capacity can be accessed, but typically at significantly higher rates.

The primary buyers of stand-alone policies have been hospitality companies, large real estate firms and financial institutions, according to Marsh. Retail companies, media entities, transportation, public entities and utilities also purchased stand-alone terrorism policies, but in lesser amounts. Companies with overseas exposures often look to the stand-alone market to provide solutions not satisfied by local government terrorism insurance schemes.

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The latest extension to the terrorism risk insurance program which eliminates any distinction between domestic or foreign acts of terrorism in the definition of a certified act of terrorism has also acted as an impetus for stand-alone markets to offer more competitive terms and conditions to insureds.

ESTIMATING POTENTIAL TERRORISM LOSSES

The fact that acts of terrorism are intentional and that the frequency and severity of attacks cannot be reliably assessed makes terrorism risk extremely problematic from the insurance standpoint. Many insurers continue to question whether terrorism risk is insurable. Large segments of the economy and millions of workers are exposed to significant terrorism risk, but the ability to determine precisely where or when the next attack may occur is limited, as is the ability to predict the type of attack.

At any given time, there is a range of viewpoints among industry analysts and national security experts on where the terrorist threat is highest and which country or location is most at risk. When it comes to estimating losses from potential terrorist attacks there also appears to be significant variability in outcomes, underscoring the degree of uncertainty associated with potential terrorist attacks.

Despite the differing viewpoints, the overall consensus appears to be that terrorism risk is an ongoing, and in some cases growing, threat. Here are some of the most recent projections and predictions on the terrorism threat:

- **Unrest in Middle East:** Since the end of 2010, political demonstrations and unrest have swept across more than a dozen countries in the Middle East and North Africa (MENA) region, including Algeria, Bahrain, Egypt, Iran, Iraq, Jordan, Kuwait, Libya, Morocco, Oman, Saudi Arabia, Syria, Tunisia and Yemen. The movement known as the Arab Spring was initially sparked by an uprising in Tunisia that began in December 2010, and ultimately led to the resignation of the country's president just three months later. The protests then spread to other countries, challenging numerous political regimes and leaderships, and leading to increased tensions in a potentially volatile region of the world. Unrest and instability in this region continues in 2013.

- **Homegrown Terrorist Threat:** Catastrophe modeler RMS notes that the Boston bombing is a strong reminder of the homegrown terrorism threat in the United States.[15] While the two brothers who are suspected to be behind the attack are of Chechen descent and one of them had in recent years visited Chechnya, both had been living in the U.S. for almost a decade and follow a

[15] Bombings at the Boston Marathon Raise Specter of Homegrown Terrorism, RMS press release, April 24, 2013.

pattern of homegrown jihadi terrorism. RMS assesses that the U.S. terrorist threat will increasingly come predominantly from such homegrown extremists and notes that due to the highly decentralized structure of such "groups", they are difficult to identify and apprehend. RMS also states that the technical expertise of such homegrown operatives will be limited, so simple conventional attacks such as IEDs will remain the preferred weapon of choice. While such weapons have limited range, they potentially can cause significant property damage and inflict numerous casualties. Such attacks will occur in densely populated areas, at a time of day selected to cause the most damage and fatalities, RMS predicts. Also in April and May 2013, a spate of letters laced with ricin, one of which was addressed to President Barack Obama, were intercepted at mail facilities in Washington, D.C., and New York City.

- **Transit System Threat:** An alleged terrorist plot to blow up a New York to Toronto passenger train was recently foiled by Canadian law enforcement officials and two suspects with links to Al-Qaeda arrested. The planned attack has renewed concerns over the potential terrorist threat to mass transit systems. Following the March 29, 2010, attacks by suicide bombers on the Moscow subway that killed 39 people, New York City Mayor Michael Bloomberg announced that the New York City Police Department (NYPD) had stepped up its patrol of the subways.

- **Maritime Threat:** Experts warn that maritime piracy terrorism continues to pose a formidable threat. On February 9, 2011, the Irene SL, a Greek-flagged very large crude carrier (VLCC) bound for the United States and carrying about 2 million barrels of crude oil worth an estimated $200 million was hijacked by Somali pirates off the coast of Oman in the northern part of the Arabian Sea. INTERTANKO managing director Joe Angelo said the hijacking marked a significant shift in the impact of the piracy crisis in the Indian Ocean: "The piracy situation is now spinning out of control into the entire Indian Ocean right to the top of the Arabian Sea over 1,000 miles from the coast of Somalia.... If piracy in the Indian Ocean is left unabated, it will strangle these crucial shipping lanes with the potential to severely disrupt oil flows to the U.S. and to the rest of the world."

- **Country Risk:** A global ranking of 197 countries by risk analyst Maplecroft published in June 2012 identifies Yemen, Somalia and Afghanistan as the countries posing the most severe risk from terrorist attacks. Localized insurgencies in the growth economies of Nigeria, the Philippines, Turkey, India and Russia, meanwhile, see them featured among 18 countries classified "extreme risk." Maplecroft's research also reveals that between

September 2011 and August 2012, the 10 most at-risk states accounted for 87 percent of worldwide terrorist attacks (7,765 of the 8,927 logged by Maplecroft and the Worldwide Incidents Tracking System (WITS), while also suffering 85 percent of the 15,219 fatalities recorded over the same period.

- **Regional Terrorism Threat:** Aon's 2013 Political Risk Map measures political risks, political violence and terrorism in 163 countries and territories to help companies assess the risk levels of exchange transfer, legal and regulatory risk, political interference, political violence, sovereign non-payment and supply chain disruption. For 2013, the map shows an increase in the number of countries with upgraded political risk ratings (where the overall country or territory risk is rated lower than the previous year). Some 13 conntries were upgraded in 2013, compared to three in 2012. The 2013 map also shows only 12 countries experiencing downgrades compared to 21 in 2012. Countries downgraded in 2013 were: Algeria, Cameroon, Chad, Ethiopia, Madagascar, Mali, Namibia, Moldova, Turkmenistan, Uzbekistan, Panama and Paragnay.

THE CYBER TERRORISM THREAT

The threat both to national security and the economy posed by cyber terrorism is a growing concern for governments and businesses around the world, with critical infrastrncture, such as nuclear power plants, transportation and utilities at risk.[16]

U.S. Homeland Security Secretary Janet Napolitano recently warned that a major cyber attack is a looming threat that could have the same type of impact as superstorm Sandy, knocking ont power to a large swathe of the Northeast.

Napolitano said a "cyber 9/11" could happen imminently and noted that critical infrastructure—including water, electricity and gas—is very vulnerable to such a strike.[17]

Earlier, in an October 2012 speech U.S. Defense Secretary Leon Panetta warned that the United States was facing a possible "cyber Pearl Harbor" scenario, and increasingly vulnerable to foreign cyber attacks on its critical infrastructure networks.

Such attacks are targeting the computer control systems that operate chemical, electricity and water plants and transportation networks, Panetta said:

[16] *Cyber Risks: The Growing Threat*, March 2013, Robert P. Hartwig and Claire Wilkinson, Insurance Information Institute (I.I.I.)
[17] *Napolitano warns of risk of major cyber attack*, Newsday, January 24, 2013.

> "An aggressor nation or extremist group could use these kinds of cyber tools to gain control of critical switches. They could, for example, derail passenger trains or even more dangerous, derail trains loaded with lethal chemicals.
>
> They could contaminate the water supply in major cities or shutdown the power grid across large parts of the country."

Panetta's speech came in the wake of a cyber attack in August 2012 on state oil company Saudi Aramco, which infected and rendered useless more than 30,000 computers.

The Department of Homeland Security received reports of some 198 attacks on critical infrastructure systems in the U.S. in 2012, a 52 percent increase on 2011.[18]

In 2011, a report from the Pentagon concluded that computer sabotage coming from another country can constitute an act of war.[19] It noted that the Laws of Armed Conflict—which guide traditional wars and are derived from various international treaties such as the Geneva Convention—apply in cyberspace as in traditional warfare.

A recent survey conducted by Tenable Network Security found that the majority of Americans fear that cyber warfare is imminent and that the country will attack or be attacked in the next decade.[20]

An overwhelming 93 percent of respondents to the survey believe that U.S. corporations and businesses are at least somewhat vulnerable to state-sponsored attacks. And 95 percent believe U.S. government agencies themselves are at least somewhat to very, vulnerable to cyber attacks.

Some 94 percent of survey respondents also say they support the President having the same level of authority to react to cyber attacks as he has to respond to physical attacks on the country.

The survey also revealed conflicting results about whether the public or private sector should be held accountable for protecting corporate networks.

[18] *As Hacking Against U.S. Rises, Experts Try to Pin Down Motive*, the New York Times, March 3, 2013
[19] *Cyber Combat: Act of War*, by Siobhan Gorman and Julian E. Barnes, the Wall Street Journal, May 30, 2011.
[20] Tenable Network Security survey, February 2013.

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Some 66 percent of respondents believe corporations should be held responsible for cyber breaches when they occur. But an almost equal number of Americans—62 percent—say government should be responsible for protecting U.S. businesses from cyber attacks.

Recent high profile attacks, such as the sabotaging of Iran's nuclear program via the Stuxnet computer worm, malicious infiltration attempts by China and the reported targeting of an Illinois water utility by a remote cyber attack from Russia, highlight the capability and breadth of the cyber risk ***(Figure 6)***.

Figure 6
CYBER RISK THREAT SPECTRUM: TERRORISM IS A CONCERN

Threat	Resources	Methods	Objectives	Examples
Nation-state, sleeper insiders	High	Highly targeted	Strategic sabotage	Stuxnet
Advanced persistent threat	High	Targeted, manual remote control	IP theft	Aurora, Ghostnet
Persistent threat	Medium	Targeted, manual remote control	IP theft, defacement	Night Dragon, "Anonymous"
Disgruntled insider with access to ICS	Low	Targeted: social engineering	Sabotage	Maroochy
Insider with access to IT network	Low	Targeted: social engineering	Sabotage	IT examples
Organized crime	Medium	Highly volume, automated	Identity theft	Zeus, Conflicker

Source: Waterfall Security Systems

A recent study by the Ponemon Institute in collaboration with Bloomberg Government estimated private sector spending on cyber security at roughly $80 billion in 2011, but noted that this was not nearly enough.

The study found that "utilities, banks and phone carriers would have to spend almost nine times more on cyber security to prevent a digital Pearl Harbor from plunging millions into darkness, paralyzing the financial system or cutting commnnications," according to a report by Bloomberg News.[21] Its findings were

[21] *Cybersecurity Disaster Seen in the U.S. Survey Citing Spending Gaps*, by Eric Engleman and Chris Strohm, Bloomberg News, January 31, 2012.

based on interviews with technology managers from 172 U.S. organizations in six industries and government.

TERRORISM RISK INSURANCE PROGRAM: STRUCTURE AND COVERAGE

The Terrorism Risk Insurance Act of 2002 was adopted by Congress to ensure the widespread availability and affordability of property and casualty insurance for terrorism risk. The act provides a temporary program, or "backstop" for incurred losses resulting from certain acts of terrorism.

The act was extended in 2005 for two years and again in 2007 for another seven years, through December 2014, under the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA). Both extensions of the act changed some components of the program, increasing the portion of the loss insurers would pay in the event of a terrorist attack and reducing the types of commercial insurance covered by the program.

It is important to note that the program provides no coverage for personal lines insurers, reinsurers and group life insurance losses (see below).

The major provisions of the terrorism risk insurance program are as follows:

- **Make available requirement:** Only commercial insurers and causes of loss specified in the underlying policies are covered under the program and required to make coverage available. Residual market insurers such as workers compensation pools, captive insurers and risk retention groups are also covered. Personal lines insurers and reinsurers are not covered; neither are group life insurance losses. Most types of commercial insurance lines were covered under the original legislation, except for some specialty coverages such as medical malpractice and crop insurance. Under the 2005 extension, certain additional lines are now excluded:
    - Commercial automobile
    - Burglary and theft
    - Surety
    - Professional liability, except for directors and officers liability
    - Farm owner multi-peril insurance
- **Definition of a certified act of terrorism:** The 2007 extension expanded the definition of a certified act of terrorism to eliminate any distinction between domestic or foreign acts of terrorism. The original act covered only acts of foreign terrorism on U.S. soil.

- **Triggering event:** The threshold for the program to go into effect rose from $5 million under the original act to $50 million after March 2006. In 2007, the triggering event threshold rose to $100 million and remained there under TRIPRA. Federal funds will be paid out only in the event of a terrorist act that produces total insurance industry losses above this threshold.

- **Program cap:** The program is capped at $100 billion per year for insured losses (federal and insurer combined). A provision in the law requires the U.S. Department of the Treasury to establish a process for the allocation of pro-rata payments in the event that terrorism-related insured losses exceed the federal government's annual $100 billion cap. The law states that no insurer may be required to make any payment for insured losses in excess of its deductible and its share of insured losses.

- **Individual insurer deductibles:** The amount of terrorism losses that an individual insnrer must pay before federal assistance becomes available. The level rose to 20 percent of an insurer's direct earned premiums for commercial property/casualty insurance in 2007 where it currently remains (up from 17.5 percent in 2006 and 15 percent in 2005).

- **Co-payments:** The share of losses that insurers pay above their individual retentions rose to 15 percent in 2007 where it remains today, up from 10 percent in 2006.

- **Industry retention level:** The industry as a whole must cover a certain proportion of the losses through deductibles and copayments before federal assistance kicks in. This amount rose to $27.5 billion in 2007 where it remains today, up from $25 billion in 2006 and $15 billion in 2005 ***(Figure 7)***. If the insured loss is less than the $27.5 billion threshold, the federal government can recoup the difference between the actual amount it paid and the required retention. This comes via a surcharge on commercial insurance policyholders not to exceed 3 percent of premium for insurance coverages that fall under the program. If the insured loss exceeds this threshold, federal expenditures may be recouped for amounts in excess of the threshold at the discretion of the Secretary of the Treasury.

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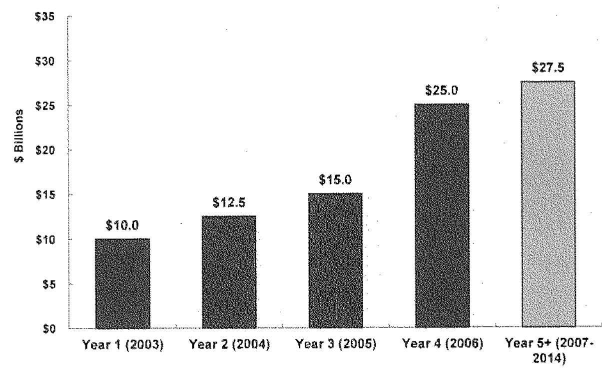
Figure 7
INSURANCE INDUSTRY RETENTIONS UNDER TRIA AND ITS SUCCESSORS
($ Billions)



Source: Insurance Information Institute.

FEDERAL ROLE IN TERRORISM INSURANCE

The Obama administration's 2011 budget plan had included a proposal seeking to scale back federal support for the terrorism risk insurance program. Its justification was that this would "encourage the private sector to better mitigate terrorism risk through other means, such as developing alternative reinsurance options and building safer buildings." The proposal projected savings of $249 million in the course of the following 10 years as a result of the reduction in federal support. However, no planned cuts to the program were included in the administration's 2014 budget plan.

Industry observers noted that any attempts to modify the program would have a detrimental effect on the availability and affordability of terrorism insurance—problems that the program was designed to end.

Studies by various organizations, including the University of Pennsylvania's Wharton School Risk Center, the RAND Corporation and the Organization for

Economic Co-operation and Development (OECD), have supported the idea of a substantive federal role in terrorism insurance. In particular, the Wharton School found that TRIA has had a positive effect on availability of terrorism coverage and also has significantly contributed to reducing insurance premiums.[22] The OECD notes that thus far the financial markets have shown little appetite for terrorism risk.

Terrorism Risk Insurance Programs in Other Countries

A number of countries have established their own terrorism risk insurance programs and these have operated successfully, often for many years. Australia, Austria, Belgium, France, Germany, the Netherlands, Spain, Switzerland and the United Kingdom have all created programs to cover terrorism in the event of an attack on their own soil ***(Figure 8)***.

In 1993, the British government formed a mutual reinsurance pool for terrorist coverage following acts of terrorism by the Irish Republican Army. Insurance companies pay premiums at rates set by the pool. The primary insurer pays the entire claim for terrorist damage but is reimbursed by the pool for losses in excess of a certain amount per event and per year. This is based on its share of the total market. The maximum industry retention increases annually per event and per year. Following 9/11, coverage was extended to cover all risks, except war, including nuclear and biological contamination, aircraft impact and flooding, if caused by terrorist attacks. The British government acts as the reinsurer of last resort, guaranteeing payments above the industry retention.

[22] *Evaluating the Effectiveness of Terrorism Risk Financing Solutions*, Howard C. Kunreuther and Erwann O. Michel-Kerjan, September 2007, National Bureau of Economic Research.

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Figure 8
COUNTRIES OPERATING COMPULSORY OR OPTIONAL TERRORISM POOLS

Country	Compulsory Pool (Y/N)	Name of Terror Pool or Reinsurance Mechanism
Australia	N	Australian Reinsurance Pool Corporation (ARPC)
Austria	N	Österreichisher Versicherungspool zur Deckung von Terrorisiken (The Austrian Terrorpool)
Bahrain	N	The Arab War Risks Insurance Syndicate (AWRIS)
Belgium	N	Terrorism Reinsurance & Insurance Pool (TRIP)
Denmark	N	Danish Terrorism Insurance Scheme
Finland	N	Finnish Terrorism Pool
France	Y	Gestion de l'Assurance et de la Réassurance des Risques d'Attentats et Terrorisme (GAREAT)
Germany	N	EXTREMUS Versicherungs-AG
Hong Kong - China	N	The Motor Insurance Bureau (MIB)
India	N	The General Insurance Corporation of India
Indonesia	N	Indonesian Terrorism Insurance Pool
Israel	Y	Terrorism (Intifada Risks) – The Victims of Hostile Actions (Pensions) Law and the Property Tax and Compensation Fund Law
Namibia	N	Namibia Special Risks Insurance Association (NASRIA)
Netherlands	N	Nederlandse Herverzekeringsmaatschappij voor Terrorismeschaden (NHT)
Northern Ireland	N	Criminal Damage Compensation Scheme Northern Ireland
Russia	N	Russian Anti-terrorism Insurance Pool (RATIP)
South Africa	N	South African Special Risks Insurance Association (SASRIA)
Spain	Y	Consorcio de Compensacion de Seguros (CCS)
Sri Lanka	N	SRCC/Terrorism Fund - Government
Switzerland	N	Terrorism Reinsurance Facility
Taiwan	N	Taiwan Terrorism Insurance Pool
United Kingdom	N	Pool Reinsurance Company Limited (Pool Re)
United States	N	Terrorism Risk Insurance Reauthorization Act of 2007 (TRIPRA)

Source: Guy Carpenter & Co, LLC

Fire Following

State law has also addressed the issue of terrorism cover. Before 9/11, 31 jurisdictions had laws that required that property policies be based on the 1943 New York Standard Fire Policy (SFP). The SFP does not exclude fire following terrorism and, prior to 2003, the SFP did not permit this exclusion with the result that a policyholder who had rejected terrorism coverage under TRIA would still have coverage for fire following an act of terrorism. Currently, this is still the case in just a handful of states.

However, since 2003, some states have revised their SFP statutes to permit exclusions of fire following terrorism under certain circumstances. Thus, for a policyholder who has rejected terrorism coverage under TRIA, in these states there might be no coverage or limited coverage for fire resulting from an act of terrorism. Many states do not have a standard fire policy statute or have SFPs that unconditionally exclude fire following terrorism. In these states there is no stipulated coverage for fire following terrorism.

NUCLEAR, BIOLOGICAL, CHEMICAL AND RADIOLOGICAL (NBCR) THREAT

Acts of terrorism have the potential to be large, destabilizing events, giving rise to losses of an unquantifiable size and severity. Potential terrorism scenarios often include the likely impact of an incident involving weapons of mass destruction (WMD).

As recently as January 2010 the U.S. Government Accountability Office (GAO) stated that a terrorist's use of either a radiological dispersal device (RDD)—frequently referred to as a "dirty bomb"—or an improvised nuclear device (IND) to release radioactive materials into the environment could have devastating consequences.[23] It noted that the consequences of a terrorist attack using an RDD or IND would include not only loss of life but also enormous psychological and economic impacts.

An April 2006 study by the American Academy of Actuaries explored the insured losses that nuclear, biological, chemical and radiological (NBCR) incidents might give rise to in four U.S. cities. It estimated that in New York a large NBCR event could cost as much as $778.1 billion, with insured losses for commercial property at $158.3 billion and for workers compensation at $483.7 billion. A loss of this magnitude is more than three times the size of the commercial P/C insurance industry's claims-paying capacity. The three other U.S. cities included in the analysis were Washington, DC; San Francisco, CA; and Des Moines, IA.

[23] *Combating Nuclear Terrorism: Actions Needed to Better Prepare to Recover from Possible Attacks Using Radiological or Nuclear Materials*, Government Accountability Office (GAO), January 2010, GAO-10-204.

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Nuclear, biological, chemical and radiological attacks are another example of catastrophic events that are fundamentally uninsurable due to the nature of the risk. The Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA) did not include an earlier controversial provision that would have required insurers to make available coverage for NBCR attacks. There are long-standing restrictions regarding war coverage and NBCR events in both personal and commercial insurance policies.

However, a June 2010 report by Guy Carpenter noted that some two-thirds of reinsurance markets surveyed are now offering coverage for NBCR events, reflecting a true evolution in underwriting appetite since 9/11.[24] An increasing number of reinsurers have entered the market over the last few years, offering new solutions for various large-scale risks such as airports, industrial plants, sports stadiums and shopping centers, Guy Carpenter said. It noted that costs of coverage vary depending on a number of factors, including geographical spread of risk, the location and type of exposure, proximity to other risks and the program's structure (e.g. limit and deductibles).

The reauthorization of the terrorism risk insurance program in 2007 directed GAO to review: the extent to which insurers offer NBCR coverage; factors that contribute to the willingness of insurers to provide NBCR coverage; and policy options for expanding coverage for NBCR risks. In its report, GAO said that commercial property/casualty insurers generally still seek to exclude NBCR coverage per long-standing exclusions for nuclear and pollution risks, although such exclusions may be subject to challenges in court because they were not specifically drafted to address terrorist attacks.[25]

GAO noted that commercial property/casualty policyholders, including companies that own high-value properties in large cities, generally reported that they could not obtain NBCR coverage. Unlike commercial P/C insurers, workers compensation, group life and health insurers reported providing NBCR coverage because states generally do not allow them to exclude these risks. GAO reviewed several proposals but made no recommendations on the NBCR issue.

[24] *Terrorism: Reinsurers Standing By*, Guy Carpenter, June 2010.
[25] *Terrorism Insurance: Status of Coverage Availability for Attacks Involving Nuclear, Biological, Chemical or Radiological Weapons*, U.S. Government Accountability Office (GAO), December 2008.

AVIATION INSURANCE FOR TERRORISM RISKS

Aviation insurance for terrorism risks continues to be an issue of concern for countries around the world. The attempted Christmas Day 2009 attack on a Northwest Airlines flight from Amsterdam to the United States by Umar Farouk Abdulmutallab, who allegedly tried to detonate plastic explosives hidden in his underwear, is one of the latest reminders that terrorists continue to look for opportunities to target international aviation.

Airlines are required to have passenger and third-party liability insurance coverage in order to receive landing rights and as a condition for leases, so the cancellation of insurance cover could affect the industry's ability to operate.[26] In the wake of 9/11, there was a complete withdrawal of coverage for acts of war, terrorism and related perils. As a result a number of governments stepped in and established schemes to temporarily fill the coverage gap. Since then, the private market has partially reinstated coverage, though at a significantly higher cost.

Some countries, like the United States, assist airlines in insuring war risks. The Federal Aviation Administration (FAA) began issuing premium third party liability war risk insurance to U.S. air carriers in the wake of 9/11. The Homeland Security Act of 2002 (HAS) and subsequent legislation mandated the expansion of war risk insurance coverage to include hull loss and passenger liability and required continued provision of the insurance.

The program has been extended several times. As of October 1, 2012, the FAA Aviation Insurance Program Office provides war risk hull loss, as well as passenger and third party liability insurance to regularly scheduled U.S. air carriers for the period through September 30, 2013.

THE LIABILITY FACTOR

Another distinguishing feature of terrorist attacks is their ability to generate enormous liability losses in addition to physical losses. In the immediate aftermath of 9/11 it became clear that thousands of victims and their families were prepared to litigate to recover economic and non-economic (e.g., pain and suffering, emotional distress, etc.) damages.

To minimize the likelihood of a wave of liability claims against the airlines and other likely litigants in the days following 9/11, Congress established the Victims Compensation Fund (VCF). The program was designed to provide a no-fault alternative to tort litigation for these individuals or relatives and provided compensation for losses due to personal physical injnries or death.

[26] *Global Terror Update 2009*, Guy Carpenter.

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By the time the VCF ceased operations on June 15, 2004, it had processed nearly 7,400 claims for death and physical injury and provided around $7 billion in payments to families of 9/11 victims. In return, victims' families were required to give up the right to sue the airlines, government agencies or other entities they perceived as responsible parties.

TRIA and its extension legislation contain no provision for handling liability claims in future. As a result, the impact of tort claims following another major terrorist attack on U.S. soil has the potential to be enormous. It is worth nothing that even with the VCF a substantial number of lawsuits were filed in the wake of 9/11. For example, recent media reports suggest that settlements have been reached in 93 of 96 wrongful death and injury lawsuits related to 9/11 and submitted to Federal District Court in Manhattan. Although the amounts are confidential, reports cite a document showing that the defendants have paid out a total of $500 million.[27]

Ground Zero Workers and Health Claims

In addition to the direct liability costs associated with terrorist attacks, ailments and illnesses contracted by workers involved in post-attack rescue and clean-up activities can increase liability losses by hundreds of millions of dollars. These types of suits will add hundreds of millions of dollars to the final cost of a major terrorist attack.

In November 2010, more than 10,000 workers whose health was damaged during the rescue and cleanup at the World Trade Center approved a settlement of at least $625 million with New York City officials. For the settlement to take effect at least 95 percent of the plaintiffs had to agree to its terms. The settlement would have paid out $712.5 million if all of the plaintiffs had opted in. According to reports, the final acceptance rate was 95.1 percent.[28]

The plaintiffs will be compensated according to the severity of their illnesses and the extent of their exposure to contaminants at the site. Under the terms of the settlement, individual payments will range from $3,250 to $1.8 million or more for the worst injuries, according to estimates from lawyers. Payouts to the plaintiffs will come from a federally financed insurance company called the WTC Captive Insurance Company with approximately $1.1 billion in funds to provide coverage to the city.

[27] *Judge's Approval Sought in 2 Lawsuits from 9/11*, by Benjamin Weiser, the New York Times, 02/05/2010
[28] *Sept. 11 Workers Agree To Settle Health Lawsuits*, by Mireya Navarro, the New York Times, 11/19/2010

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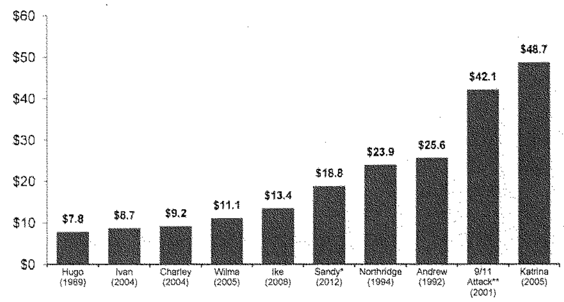
CONCLUSION

The cost of terrorism still looms large in United States history. The $32.5 billion in losses ($42.1 billion in 2012 dollars) paid out by insurers for the terrorist attack of September 11, 2001, places second in an Insurance Information Institute (I.I.I.) ranking of the most costly U.S. catastrophes—just after Hurricane Katrina (2005) ***(Figure 9)***.

More than a decade later, 9/11 also remains the worst terrorist act in terms of fatalities and insured property losses.

Figure 9
THE TEN MOST COSTLY CATASTROPHES, UNITED STATES (1)
(Insured Losses, 2012 dollars, $ billions)



*ISO estimate as of January 2013
** Insured loss estimate for Sep. 11 terrorist attack includes property, business interruption, workers comp, aviation hull, liability, event cancellation and life insurance losses.

Source: ISO's Property Claim Services unit (PCS); Insurance Information Institute inflation adjustments to 2012 dollars using the CPI.

The April 2013 Boston bombing—the first successful terror attack on U.S. soil since 9/11—underscores the fact that, while the risk is changing, terrorism is a constant threat for the foreseeable future.

Failure to focus on and prepare for this threat will come at an enormous cost to the millions of individuals and businesses who rely on insurance contracts to offset the overall economic impact of a terrorist attack.

Meanwhile, the looming expiration at the end of 2014 of the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA), brings to a head the question of whether terrorism risk now, or ever, will be one that can he managed entirely within the private sector.

Industry research suggests that market stability in terms of both pricing and availability of terrorism coverage, as well as the ability to maintain adequate and expanding levels of capacity over time, is contingent on the continued existence of the Terrorism Risk Insurance Program.

For property/casualty insurers, the increasing share of losses that they would have to fund in the event of a major terrorist attack on U.S. soil suggests that now is the time to take stock of their terrorism exposures.

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Appendix I

FAQ: TERRORISM INSURANCE—WHAT IT IS AND WHAT IT COVERS

Terrorism insurance provides coverage to individuals and businesses for potential losses due to acts of terrorism.

Businesses

Prior to 9/11, standard commercial insurance policies included terrorism coverage as part of the package, effectively free of charge. Today, terrorism coverage is generally offered separately at a price that more adequately reflects the current risk.

Insurance losses attributable to terrorist acts under these commercial policies are insured by private insurers and reinsured or "backstopped" by the federal government pursuant to the Terrorism Risk and Insurance Act of 2002 (TRIA). TRIA has been renewed twice, and the current law, known as the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA) runs until December 2014. Under the program, owners of commercial property, such as office buildings, factories, shopping malls and apartment buildings, must be offered the opportunity to purchase terrorism coverage.

Individuals

Standard homeowners insurance policies include coverage for damage to property and personal possessions resulting from acts of terrorism. Terrorism is not specifically referenced in homeowners policies. However, the policy does cover the homeowner for damage due to explosion, fire and smoke—the likely causes of damage in a terrorist attack.

Condominium or co-op owner policies also provide coverage for damage to personal possessions resulting from acts of terrorism. Damage to the common areas of a building like the roof, basement, elevator, boiler and walkways would only be covered if the condo/co-op board has purchased terrorism coverage.

Standard renters policies include coverage for damage to personal possessions due to a terrorist attack. Again, coverage for the apartment complex itself must be purchased by the property owner or landlord.

Auto insurance policies will cover a car that is damaged or destroyed in a terrorist attack only if the policyholder has purchased "comprehensive" coverage. Most people who have loans on their cars or lease are required by lenders and leasing companies to carry this optional form of coverage. People who buy liability coverage only are not covered in the event their vehicle is damaged or destroyed as the result of a terrorist attack.

Life insurance policies do not contain terrorism exclusions. Proceeds will be paid to the beneficiary as designated on the policy.

Under What Circumstances Is There Coverage?

For the terrorism coverage to be triggered under TRIPRA for commercial policies, a terrorist attack has to be declared a "certified act" by the Secretary of the Treasury.

No such declaration is needed to trigger coverage under homeowners and auto policies because there are no exclusions for terrorism.

In some states a doctrine know as "fire following" applies. This means that in the event of a terrorist-caused explosion followed by fire, insurers could be liable to pay out losses attributable to the fire (but not the explosion) even if a commercial property owner had not purchased terrorism coverage. Insurers have sought to limit fire coverage resulting from a terrorist attack, because commercial policyholders that choose to reject TRIPRA or other terrorism coverage are effectively paying no premium for the protection offered by fire-following coverage. Currently, there is coverage for fire following an act of terrorism in just a haudful of states.

What Is Not Covered?

There are long-standing restrictions regarding war coverage and nuclear, biological, chemical and radiological (NBCR) events in both personal and commercial insurance policies.

War-risk exclusions reflect the realization that damage from acts of war is fundamentally uninsurable. No formal declaration of war by Congress is required for the war risk exclusion to apply. Nuclear, biological, chemical and radiological attacks are another example of catastrophic events that are fundamentally uninsurable due to the nature of the risk.

Under the terrorism risk insurance program, if some NBCR exclusions are permitted by a state, an insurer does not have to make available the excluded coverage.

Business Interruption Insurance

Property damage to commercial buildings from a terrorist attack also may include claims for business interruption. Business interruption insurance (sometimes referred to as business income coverage) covers financial losses that occur when a firm is forced to suspend business operations either due to direct damage to its premises or because civil authorities limit access to an area after the attack and those actions prevent entry to the business premises. Coverage depends on the individual policy, but typically begins after a waiting period or "time deductible" of two to three days and lasts for a period of two weeks to several months.

Business interruption losses associated with acts of civil authority (e.g., closure of certain area around the disaster) can only be triggered when there is physical loss or damage arising from a covered peril (e.g., explosion, fire, smoke, etc.) within the area affected by the declaration. The loss/damage need not occur to the insured premises specifically. Reductions in business income associated with fear of traveling to a location, in addition to closure to areas by authorities because of a heightened state of alert, would not be covered by business interruption policies.

Workers Compensation and Other Coverages

Workers compensation—a compulsory line of insurance for all businesses—covers employees injured or killed on the joh and therefore automatically includes coverage for acts of terrorism. Workers compensation is also the only line of insurance that does not exclude coverage for acts of war. Coverage for terrorist acts cannot be excluded from workers compensation policies in any state.

There are essentially three types of workers compensation benefits. The first reimburses workers for lost wages while tbey recover from their injuries. The second covers workers for all medical expenses incurred as a result of the injuries they sustain. The third type of benefit provides payments to the families of workers killed on the job.

Life/health and disability insurance policies may provide coverage for loss of life, injury or sickness to individuals in the event of a terrorist attack.

What Is the Terrorism Risk Insurance Act (TRIA)/Terrorism Risk Insurance Program Reauthorization Act (TRIPRA)?

TRIA is a public/private risk-sharing partnership between the federal government and tbe insurance industry. The program is designed to ensure that adequate resources are available for businesses to recover and rebuild if they become the victims of a terrorist attack.

TRIA was extended for another two years in December 2005 and for another seven years to 2014 in December 2007. The new law is known as the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) of 2007.

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Specific provisions of the legislation are:

- An event must cause at least $100 million in aggregate property and casualty insurance losses to be certified by the Secretary of the Treasury as an act of terrorism.

- The definition of a certified act of terrorism has been expanded to cover both domestic and foreign acts of terrorism.

- Each participating insurer is responsible for paying out a certain amount in claims (a deductible) before federal assistance becomes available.

- For losses above a company's deductible, the federal government will cover 85 percent, while the insurer contributes 15 percent.

- The aggregate insurance industry retention in 2007 was $27.5 billion, up from $25 billion in 2006 and $15 billion in 2005.

- Losses covered by the program are capped at $100 billion.

- Lines originally excluded from the program are: personal lines (auto and home), reinsurance, federal crop, mortgage guaranty, financial guaranty, medical malpractice, flood insurance provided under the NFIP and life and health. Additional lines now excluded are: commercial auto, professional liability except for directors and officers liability, surety, burglary and theft, and farmowners multi-peril insurance.

- The Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) of 2007 is due to sunset on December 31, 2014.

Does the Terrorism Risk Insurance Program Affect the Availability and Price of Coverage?

Yes, by sharing potential losses from terrorist attacks between private insurers and the government, the terrorism risk insurance program has brought much needed additional capacity to the terrorism market. Before the program existed, businesses were left with little or no terrorism coverage, but since it came into effect they are able to purchase the cover they need.

Terrorism coverage is very difficult to price because the frequency and severity of an attack is so unpredictable. Pricing of terrorism coverage varies according to the individual risk (based on factors such as location and industry, for example), but it

INSURANCE INFORMATION INSTITUTE

is clear that the terrorism risk insurance program has had a stabilizing influence on the market.

Does an Insurer Have to Make Terrorism Coverage Available?
Yes. Under TRIPRA, all property/ casualty insurers in the U.S. are required to make terrorism coverage available. The "make available" provision applies to commercial lines of P/C insurance. Insurers are required to make an offer of coverage for "certified acts" to policyholders. If the insured rejects an offer, the insurer may then reinstate a terrorism exclusion.

What if Terrorism Coverage Is Not Purchased and a Loss Occurs?
A business that has not purchased TRIPRA or other terrorism coverage will uot be covered for damage caused to their property by a terrorist attack. An individual who has homeowners or renters coverage may be covered, according to the individual terms of their policy.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR MARK KIRK FROM PETER J. BESHAR

Q.1. Members of the property and casualty (P&C) insurance industry range widely in size and scope. Some of the largest insurers note the $100 million minimum could be increased as one means of increasing private capital standing in front of the Government. They make similar remarks about the deductible. The concern raised about this prospect, however, is that it would preclude many of the smaller insurance providers from offering terrorism risk insurance. Is there a way to ensure that smaller insurance companies are able to continue to offer terrorism insurance while also increasing either the $100 million threshold or increasing deductibles?

A.1. Did not respond by publication deadline.

Q.2. Are there ways to fine-tune the TRIA program to better serve the marketplace and help with pricing? Particularly, would it be appropriate to apply different risk profiles to the different covered lines under the program? Do all cover covered lines present the same potential exposure and are all the currently covered lines necessary for such a backstop?

A.2. Did not respond by publication deadline.

Q.3. I understand the complexity and the differences between trying to price terrorism risk compared with most other kinds of risks. Litigation, medical considerations, and employer issues can stretch out for years, and can be quite costly to the parties involved—a great example of this being worker's compensation policies, which are covered in a terrorism event and often dwarf other claims, such as those for infrastructure. Would differentiating and requiring insurance companies to cover specific lines of risks or to allow for different deductibles for different product lines seem feasible? Why or why not? Could the program that differentiates between risk profiles allow a lower deductible for higher risk profiles and higher deductibles for more manageable risk?

A.3. Did not respond by publication deadline.

Q.4. Is there increased capacity of reinsurers in the marketplace and if so, why is the increased capacity of reinsurers not being used for terrorism risk? What has your research shown with regard to the reinsurance market? What about a risk transfer mechanism to the capital markets (*i.e.,* such as terrorism bonds?).

A.4. Did not respond by publication deadline.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR MARK KIRK FROM ERWANN O. MICHEL–KERJAN

Q.1. Across most other Federal insurance programs we see the Government's inability to correctly price risk. In most circumstances of insurance, I would much prefer to see the private market model, price, and assume risk. Can you explain why the private market has been unable to effectively model and price terrorism risk since the September 11th terrorist attacks?

A.1. Did not respond by publication deadline.

Q.2. In the wake of September 11th, the Federal Government took considerable measures to better understand and prevent terrorist attacks. I know that private industry has also worked to better understand the risks associated with terrorism and how to measure and price that risk. What advances has the private market made in its ability to price this risk? What is the state of the capital markets for terrorism risk?

A.2. Did not respond by publication deadline.

Q.3. Are there ways to fine-tune the TRIA program to better serve the marketplace and help with pricing? Particularly, would it be appropriate to apply different risk profiles to the different covered lines under the program? Do all cover covered lines present the same potential exposure and are all the currently covered lines necessary for such a backstop?

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A.4. Did not respond by publication deadline.

Q.5. Is there increased capacity of reinsurers in the marketplace and if so, why is the increased capacity of reinsurers not being used for terrorism risk? What has your research shown with regard to the reinsurance market? What about a risk transfer mechanism to the capital markets (*i.e.,* such as terrorism bonds?).

A.5. Did not respond by publication deadline.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR MARK KIRK FROM ROBERT P. HARTWIG

Q.1. In the wake of September 11th, the Federal Government took considerable measures to better understand and prevent terrorist attacks. I know that private industry has also worked to better understand the risks associated with terrorism and how to measure and price that risk. What advances has the private market made in its ability to price this risk? What is the state of the capital markets for terrorism risk?

A.1. Did not respond by publication deadline.

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A.2. Did not respond by publication deadline.

Q.3. Are there ways to fine-tune the TRIA program to better serve the marketplace and help with pricing? Particularly, would it be appropriate to apply different risk profiles to the different covered lines under the program? Do all cover covered lines present the same potential exposure and are all the currently covered lines necessary for such a backstop?

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A.5. Did not respond by publication deadline.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

PREPARED STATEMENT OF BENJAMIN M. LAWSKY

SUPERINTENDENT OF FINANCIAL SERVICES, NEW YORK STATE

SEPTEMBER 25, 2013

I would like to thank Chairman Johnson, Ranking Member Crapo, and Senator Schumer for the opportunity to submit comments on the importance of reauthorizing the Terrorism Risk Insurance Act (TRIA). I would also like—in particular—to recognize Senator Schumer for his leadership on this issue, which is so vital to his constituents in New York.

Reauthorizing TRIA is critical to the health our Nation's economy. If Congress fails to act, it would cause significant disruptions in the insurance market and for the broader business community. In addition, it could jeopardize a number of important construction projects and the jobs that come with them—not only in New York, but across the country.

As the Superintendent of Financial Services at the New York State Department of Financial Services, I can attest to the fact that we in New York are unfortunately all too well acquainted with the risk of terrorism. Not only did our State endure the horror of 9/11, but we also experienced the truck bomb that in 1993 exploded at the World Trade Center and, more recently, saw the foiling of a 2010 plot to explode a bomb in Times Square. Of course, as the 1,776-foot-tall Freedom Tower and all the rebuilding around it shows, New Yorkers are incredibly resilient and enterprising.

That post-9/11 rebuilding is still in progress 12 years later, though, demonstrates how exceedingly costly, complicated, and time-consuming it can be to recover from acts of terrorism. And given that the possibility of terrorist acts in this country will always remain a reality, builders of large and iconic structures depend on terrorism insurance. TRIA ensures the availability and relative affordability of terrorism insurance coverage.

No one can forecast the frequency or severity of terrorist attacks from past experience. This fact means that it is actuarially infeasible to price accurately for terrorism coverage. For that reason, the United States and 22 other countries have implemented some form of public-private partnership for insuring against terrorism risk.

Because an insurer under New York law cannot exclude coverage for the risk of terrorism from a commercial property/casualty policy, the only way for an insurer to moderate its terrorism risk, absent TRIA, is to decline to insure property altogether. If Congress fails to reauthorize TRIA, insurance capacity in the market would dry up, which would be devastating to businesses with higher levels of terrorism risk, such as commercial construction companies.

The consequences of a constricted market for commercial property/casualty insurance would be grave. Businesses that could not find or afford sufficient coverage would have to self-insure against property damage and liability, and banks would refuse to make construction loans to builders that carried insufficient levels of property/casualty insurance. Rebuilding from the destruction of 9/11 and, more recently, from Superstorm Sandy, would grind to a halt for those without coverage.

TRIA's impacts are not limited to property risk alone. Because workers compensation coverage by law cannot be capped, an insurer writing such risk without the kind of protection afforded by TRIA faces unquantifiable liability if a business with a significant number of employees were to suffer significant injuries and/or loss of life. In fact, the uncertainty about whether TRIA will be reauthorized already is affecting the appetite of insurers to write workers compensation insurance beyond December 31, 2014, the date by which TRIA currently is set to expire.

Simply put, TRIA provides a critical backstop that encourages insurance companies to underwrite terrorism risk responsibly, and makes it possible for carriers to offer terrorism coverage that is relatively affordable for businesses. And unlike other Federal disaster assistance programs like the National Flood Insurance Program, Federal support under TRIA only kicks in once a certified act of terrorism has caused insurers, in the aggregate, to pay losses in excess of a threshold amount and to pay additional losses to the extent of a deductible equaling a percentage of their premiums written. The TRIA program then covers a percentage of losses (insurers cover the remainder), and only then up to a capped amount. This sophisticated structure is a prudent public-private solution that brings certainty to the marketplace for a difficult-to-quantify risk.

To help ensure that the insurance marketplace operates in an efficient and affordable fashion, we urge Congress not only to reauthorize TRIA, but to make it permanent. Doing so will avoid the market upheaval that occurred in the past when TRIA's prior expiration dates approached, and provide the certainty that insurers and businesses need in this post-9/11 world.

AMERICAN HOTEL & LODGING ASSOCIATION
Washington, DC 20005, September 24, 2013

Hon. TIM JOHNSON
Chairman
Senate Committee on Banking, Housing, and Urban Affairs
Washington, DC.

Hon. MICHAEL CRAPO
Ranking Member
Senate Committee on Banking, Housing, and Urban Affairs
Washington, DC.

Dear Chairman Johnson and Ranking Member Crapo:

The American Hotel & Lodging Association applauds the leadership of the Senate Banking Committee in holding hearings to consider the Terrorism Risk Insurance Program Reauthorization Act of 2007 (TRIPRA). The lodging industry calls on Congress to act quickly to continue this important private/public partnership.

AH&LA is a 100-year-old association of State and city partner lodging associations throughout the United States with some 10,000 property members nationwide. We represent more than 4.9 million guest rooms and over 1.8 million employees in the United States. AH&LA's membership ranges from the smallest independent properties to the largest convention hotels.

Without TRIPRA, the lodging industry will face substantial difficulty in obtaining terrorism risk coverage which is often required for securing loans for development projects. The Terrorism Risk Insurance Act (TRIA) was enacted in the months following the September 11, 2001 attacks and provides a Federal plan for economic continuity and recovery in the event of another severe terrorist attack against the United States. TRIPRA ensures a market exists for businesses to secure terrorist risk coverage often required under the terms of bank loans. Importantly, TRIPRA protects American taxpayers as the program mandates that "first dollar losses" be paid by insurers and policy holders and is only triggered in the event of a major event and after individual insurer loss thresholds are met. In addition, the program has operated virtually cost-free to the taxpayer since being enacted.

The lodging industry has seen no evidence that the terrorism risk market is prepared to provide coverage without the private/public partnership TRIPRA provides. TRIPRA has allowed for terrorism coverage prices to stabilize and adequate coverage to be secured with minimal risk to taxpayers. Our members will soon begin to see renewal notices with exclusion clauses if TRIPRA is not renewed by Congress.

AH&LA applauds your efforts to extend this vital program and calls on Congress to act quickly.

Thank you for your consideration of our views.

Sincerely,

KATHERINE G. LUGA,
President and CEO

Cc: Members of Senate Banking, Housing, and Urban Affairs Committee

CHAMBER OF COMMERCE
OF THE
UNITED STATES OF AMERICA

R. BRUCE JOSTEN
EXECUTIVE VICE PRESIDENT
GOVERNMENT AFFAIRS

1615 H STREET, N.W.
WASHINGTON, D.C. 20062-2000
202/463-5310

September 24, 2013

The Honorable Tim Johnson
Chairman
Committee on Banking, Housing, and
Urban Affairs
United States Senate
Washington, DC 20510

The Honorable Mike Crapo
Ranking Member
Committee on Banking, Housing, and
Urban Affairs
United States Senate
Washington, DC 20510

Dear Chairman Johnson and Ranking Member Crapo:

The U.S. Chamber of Commerce, the world's largest business federation representing the interests of more than three million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations, and dedicated to promoting, protecting, and defending America's free enterprise system, thanks you for holding a hearing on "Reauthorizing TRIA: The State of the Terrorism Risk Insurance Market."

In the months following the 9/11 terrorist attacks, the inability for insurance policyholders to secure terrorism risk insurance contributed to a paralysis in the economy, especially in the construction, travel and tourism, and real estate finance sectors. Since its initial enactment in 2002, TRIA has served as a vital public-private risk sharing mechanism, ensuring that private terrorism risk insurance coverage remains commercially available and that the U.S. economy would more swiftly recover in the event of a terrorist attack.

Catastrophic terrorism remains an uninsurable risk because its frequency and location cannot be accurately predicted, and its potential scale could be devastating. Without the backstop that TRIA provides, the private insurance market would be unable to provide adequate levels of terrorism risk insurance. TRIA promotes long-term availability of terrorism risk insurance for catastrophic terror events and has provided a standard of stability for financial markets and recovery after such an attack.

While TRIA is currently set to expire at the end of 2014, the Chamber strongly urges Congress to reauthorize this program sooner rather than later. As the Chamber's member companies map out plans for the next 16 months and beyond, the ability to secure terrorism risk insurance is crucial to ensuring that the American business community has the certainty that it needs to continue to move forward with projects and create jobs.

The Chamber thanks you again for holding this hearing and looks forward to working with the Committee to secure swift reauthorization of this important program.

Sincerely,

R. Bruce Josten

R. Bruce Josten

cc: Members of the Committee on Banking, Housing, and Urban Affairs

The Real Estate Roundtable

September 24, 2013

The Honorable Tim Johnson
Chairman
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, DC 20510

The Honorable Mike Crapo
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, DC 20510

Dear Chairman Johnson and Ranking Member Crapo:

We are writing to thank you for holding a hearing to address the important issue of extending the nation's federal terrorism risk insurance plan, as established by the Terrorism Risk Insurance Act of 2002 (TRIA) and its subsequent extensions.

For more than a decade, TRIA has made it possible for businesses to purchase the terrorism risk coverage they need at almost no cost to the taxpayer. TRIA helps private markets provide the U.S. economy with the coverage it needs, while protecting the taxpayer. While TRIA was originally intended to be a temporary measure – a bridge to a time when reinsurers returned to the market place – there have been no developments over the last 12 years that have permitted the reinsurance industry to improve their ability to effectively quantify the unique and catastrophic risks associated with terrorism. There is no evidence that TRIA is crowding out private insurance players; private markets are just not able to provide the necessary market capacity to sustain the U.S. economy.

Terrorism continues to pose a threat to our nation, to American businesses and to real estate. Real estate plays a dominant role in the nation's economy, and it is the one sector that terrorists have successfully attacked. Real estate is especially vulnerable due to the large inventory of buildings across the nation that are populated by large numbers of people on a daily basis. As taxpayer funds are used to *harden* government targets, more *soft targets* in the private sector become vulnerable – despite the hundreds of millions of dollars spent on enhanced security measures and risk mitigation by the private sector since 9/11. Without adequate terrorism insurance coverage, our economy, our jobs, and our well-being become more vulnerable to the designs of the terrorists who hope to destroy our economic strength. Economic security is central to homeland security. It is what terrorists are targeting.

As 2013 draws to a close, annual commercial insurance policies covering businesses of all sizes and types are set to renew. Those policyholders with terms extending past TRIA's December 31, 2014 sunset date are being told to expect conditional terrorism exclusions – raising grave concerns about potentially devastating gaps in coverage. In fact, the two top headwinds we see to economic growth and job creation concern monetary policy changes – how and when interest rates rise – and the ability to obtain terrorism insurance – without which transactions of all size and product type will be slowed or cancelled.

Market Square West • 801 Pennsylvania Ave., NW • Suite 720 • Washington, DC 20004 • Phone: 202-639-8400 • Fax: 202-639-8442 • www.rer.org

September 24, 2013
Page 2

The staggering economic impact of this market condition must not be forgotten. A Real Estate Roundtable study of the 14-month post-9/11, pre-TRIA period revealed that more than $15 billion in real estate related transactions were either stalled or cancelled because of a lack of terrorism insurance. The White House Council of Economic Advisors concluded that approximately 300,000 jobs were lost during that period. TRIA was intended to ensure that the economy was strong enough to withstand a future attack. That purpose remains as important today as it was in November 2002.

With the nation's terrorism risk insurance plan set to expire in 2014, now is the time for Congress to address the problem and enact a long-term solution. We look forward to working constructively with the Committee to move this measure forward.

Sincerely,

Jeffrey D. DeBoer
President and Chief Executive Officer

cc: Members of the Senate Banking Committee

PCI

Property Casualty Insurers
Association of America
Advocacy. Leadership. Results.

Property Casualty Insurers Association of America (PCI)

Committee on Banking, Housing and Urban Affairs
United States Senate
September 25, 2013

The Property Casualty Insurers Association of America (PCI) commends Chairman Johnson, Ranking Member Crapo and the Senate Banking, Housing, and Urban Affairs Committee for holding this hearing on the Terrorism Risk Insurance Act of 2002 (TRIA). PCI is composed of more than 1,000 member business, home and auto insurance companies, representing the broadest cross-section of any national insurance trade association. PCI members write more than $195 billion in direct premium, which is 39 percent of the nation's property-casualty insurance.

As explained more fully in PCI's recent comments to the President's Working Group on Financial Markets (see attached), having a federal terrorism insurance plan in place prior to another catastrophic terrorism event is critical to protect America's economic resiliency. TRIA ensures that businesses can continue to obtain terrorism coverage necessary to protect their economic activity and obtain ongoing financing, while being fiscally responsible for taxpayers by limiting any federal involvement only to catastrophic terrorist attacks certified as being intended to coerce the civilian population or influence the U.S. government. Not a penny from the terrorism risk insurance plan ultimately goes to insurers. Any federal shared responsibility only kicks in after insurers have exhausted their deductibles and exceeded high level triggers, at which point TRIA limits insurance liabilities and provides a backstop protection to policyholders, with a recoupment mechanism in place to make the government whole over time.

There are several risks (such as war risk and more recently terrorism risk) that are not broadly insurable in the private market and are not naturally susceptible to spreading across a limited number of private parties. Terrorism risk does not fall within any of the traditional definitions of insurability and absent a finite limit on liability to mitigate aggregate risk exposures, private investors and insurers cannot responsibly commit capital beyond a limited specialty niche. The current terrorism risk insurance plan already requires insurer liability for terrorism far beyond the private sector appetite, with most insurers trying to manage their probable maximum loss exposures far below the caps that TRIA provides. The termination of TRIA or increases in insurers' obligations under the program (through the deductibles, co-shares, triggers and caps) could have devastating effects on the market as the increased risk could cause private capital to recede and credit rating agencies and insurance regulators would further pressure carriers to reduce their underwriting exposure to maintain solvency. Indeed, the insurance broker AON has said they expect "a withdrawal of insurance capacity for terrorism and a reversion to a post-9/11 environment," should TRIA be allowed to lapse.[1] This could have the undesired effect of reducing the availability of commercial coverages, which would run counter to one of the key purposes of the TRIA program as set forth in the statute: "To protect consumers by addressing market disruption and ensure the continued widespread availability and affordability of property and casualty insurance for terrorism risk."

TRIA is especially important to the workers compensation market due to the mandatory nature of the coverage. Workers compensation insurers cannot exclude terrorism. So without TRIA, some workers compensation insurers would likely face rating agency pressures, which could effectively force them to reduce their exposures. If fewer commercial insurers are in the market, this could put added pressure on states, all of which provide either a residual market mechanism or a state fund as a market of last resort. State taxpayers could become responsible for state fund liabilities, and because any remaining insurer participants in a state are assessed to capitalize state residual market mechanisms, this may also leave them with no choice but to reduce exposures further.

One of TRIA's best attributes is that it keeps commercial insurers participating in the terrorism insurance market, thus protecting taxpayers from most terrorism losses. Commercial insurers pay losses through their annual TRIA deductibles and then additional co-pays even if federal payments are made. Over the past twelve years, the commercial industry's participation in writing terrorism risks has gradually increased under TRIA. While there is a limit to the capital the commercial market can commit to underwriting terrorism risk, the Congress wisely designed the program to keep the maximum amount of private capital at work in the market, reserving a government role only for catastrophic events that commercial insurers simply cannot handle alone.

In addition, when federal payments are made, taxpayers are protected by a mechanism that allows federal payments to be recouped from the insurance marketplace. And this recoupment is mandatory for all but the largest of losses.

Taken together, these two features make TRIA an extraordinarily fiscally responsible program.

TRIA currently provides an economic and national security terrorism resiliency plan that has been extremely successful in protecting the United States. It has cost taxpayers nothing in loss payments and negligible administrative costs while improving the availability of private capital and terrorism insurance in the marketplace to keep our economy moving forward.

PCI, its members and their policyholders strongly support the current terrorism risk management plan and encourage your consideration of a long-term reauthorization to provide stability and certainty in the marketplace. Although Treasury has not certified a

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[1] *Reinsurance Market Outlook*, AON Benfield, September 2013, p. 28.

terrorist event since TRIA's inception, having a terrorism protection plan in place before the next event occurs continues to be essential for all businesses, small and large, to manage their risk and obtain financing for ongoing economic activity. The federal government has greatly expanded its efforts to interdict terrorist attacks and protect national security but TRIA is an essential plan to mitigate loss liabilities and stabilize the markets if a catastrophic event occurs. Since a key objective behind terrorist attacks is to destroy or damage the U.S. political and economic systems, including critical infrastructure, the federal government must remain an integral part of any comprehensive terrorism risk management strategy in order to protect national security and the country's financial well-being.

We look forward to working with the Committee to help satisfy all members of the Congress that the program will continue to function as a fiscally responsible and effective national terrorism risk management plan that maximizes private sector participation and protects taxpayers.

NMHC National Multi Housing Council
Apartments: Smart Communities, Smarter Living

NAA National Apartment Association

September 24, 2013

The Honorable Tim Johnson
Chairman
Senate Committee on Banking, Housing and Urban Affairs
Washington, D.C. 20510

The Honorable Mike Crapo
Ranking Member
Senate Committee on Banking, Housing and Urban Affairs
Washington, D.C. 20510

Dear Chairman Johnson and Ranking Member Crapo:

On behalf of the National Multi Housing Council (NMHC) and the National Apartment Association (NAA) we applaud your leadership in holding this hearing on "Reauthorizing TRIA: the State of the Terrorism Risk Insurance Market." With the current program set to expire next year, we are encouraged by the Committee's efforts to evaluate the effectiveness of the program as well as efforts to reauthorize the Act.

NMHC/NAA represent the nation's leading firms participating in the multifamily rental housing industry. Our combined memberships engage in all aspects of the apartment industry, including ownership, development, management and finance. NMHC represents the principal officers of the apartment industry's largest and most prominent firms. NAA is a federation of 170 state and local apartment associations comprised of approximately 60,000 multifamily housing companies representing more than 6.6 million apartment homes throughout the United States and Canada.

The Terrorism Risk Insurance Act (TRIA) and subsequent extensions of the program have been the mechanism that provides ready access to affordable terrorism coverage for apartment property owners, developers and managers across the country. The federal government's involvement has been the key factor to ensuring availability of insurance for terrorist events. Terrorism risk does not resemble any other commercial risk. Unlike natural disasters in which insurers have had significant experiences and data to project the risk of damage, terrorism is unpredictable. The impact can be enormous, and insurance modeling for such risks is still not reliable, thus underscoring the importance of continued federal involvement.

The NMHC conducts an annual survey to capture insurance costs, limits, deductibles, etc. for apartment properties. Data is generally collected from approximately 60-70 member companies representing over one million apartment units nationwide. Overall, take up rates for the apartment sector have always been one of the highest reported among commercial property types. The 2011 results report 85% of apartment firms surveyed purchased terrorism coverage as part of their property program. This is not insignificant and demonstrates that certainty in costs and coverage limits are critical components in a multifamily property owner's continued ability to offer safe and affordable housing

As you consider the proposals before you today we ask that you work expeditiously. If TRIA is allowed to lapse, businesses will once again be unable to secure coverage for catastrophic terrorism. The short term interruptions that result with looming expiration dates are harmful to the overall health of the economy.

We believe the federal government should continue in its role to ensure that terrorism risk insurance is available and affordable for all American businesses while continuing to explore options for a future private market solution. We urge you to reauthorize the TRIA beyond its 2014 expiration and we look forward to working with you.

Thank you.

Sincerely,

Douglas M. Bibby
President
National Multi Housing Council

Douglas S. Culkin, CAE
President
National Apartment Association

NATIONAL CONFERENCE *of* STATE LEGISLATURES

The Forum for America's Ideas

RESOLUTION IN SUPPORT OF THE FURTHER EXTENSION OF THE TERRORISM RISK INSURANCE ACT OF 2002

NCSL STANDING COMMITTEE ON COMMUNICATIONS, FINANCIAL SERVICES & INTERSTATE COMMERCE

WHEREAS, the United States continues to be engaged in an ongoing war against terrorism and the threats of future attacks inside the country remains; and

WHEREAS, future attacks could include the use of unconventional (nuclear, biological, chemical or radiological) weapons that could result in a large number of casualties or could involve attacks such as cyber-terrorism that would impact businesses and critical infrastructure across the nation; and

WHEREAS, the Terrorism Risk Insurance Program, created through the enactment of the Terrorism Risk Insurance Act (TRIA) of 2002 and extended in 2005 and 2007, has allowed for a viable and stable terrorism risk insurance market; and

WHEREAS, absent extension by Congress, the Terrorism Risk Insurance Act of 2002 will expire on December 31, 2014; and

WHEREAS, failure by Congress to extend TRIA would likely result in the inability of insurers to offer widespread coverage for future catastrophes resulting from terrorism or would likely create capacity concerns where terrorism coverage must be provided; and

WHEREAS, without adequate terrorism insurance coverage, banks may be unwilling to extend loans for commercial transactions, such as mortgages, construction projects and other capital-intensive initiatives; and

WHEREAS, the lack of private terrorism insurance to cover losses from future terrorist attacks may require the federal government to cover such losses; and

WHEREAS, without the shared public-private responsibility program established by the Terrorism Risk Insurance Act of 2002, a limited availability of insurance against terrorism would have a severe adverse effect on our country's economy as financiers might be reluctant to lend, businesses might be reluctant to invest, and commercial consumers might be unable to afford insurance; and

WHEREAS, the Terrorism Risk Insurance Program is an essential component of effective national economic recovery following a catastrophic terrorist attack in the United States; and

WHEREAS, NCSL supported the enactment of the Terrorism Risk Insurance Act of 2002 and subsequent extensions in 2005 and 2007;

NOW, THEREFORE, BE IT RESOLVED, that NCSL supports a long-term extension of the Terrorism Risk Insurance Act of 2002; and

NOW, THEREFORE, BE IT FURTHER RESOLVED, NCSL urges Congress and the Administration to take action as soon as possible to extend the Terrorism Risk Insurance Act of 2002.

Adopted at NCSL General Business Meeting, August 2013.

NATIONAL CONFERENCE OF INSURANCE LEGISLATORS

Resolution in Support of the Further Extension of the Terrorism Risk Insurance Act of 2002

Adopted by the NCOIL Executive Committee on July 14, 2013, and State-Federal Relations Committee on July 11, 2013. ***Sponsored by Rep. Michael Stinziano, OH***

WHEREAS, the United States continues to be engaged in an ongoing war against terrorism and the threats of future attacks inside the country remains; and

WHEREAS, future attacks could include the use of unconventional (nuclear, biological, chemical or radiological) weapons that could result in a large number of casualties or could involve attacks such as cyber-terrorism that would impact businesses and critical infrastructure across the nation; and

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WHEREAS, without the shared public-private responsibility program established by the Terrorism Risk Insurance Act of 2002, a limited availability of insurance against terrorism would have a severe adverse effect on our country's economy as financiers might be reluctant to lend, businesses might be reluctant to invest, and commercial consumers might be unable to afford insurance; and

WHEREAS, the Terrorism Risk Insurance Program is an essential component of effective national economic recovery following a catastrophic terrorist attack in the United States; and

WHEREAS, NCOIL supported the enactment of the Terrorism Risk Insurance Act of 2002 and subsequent extensions in 2005 and 2007;

NOW, THEREFORE, BE IT RESOLVED, that NCOIL supports a long-term extension of the Terrorism Risk Insurance Program; and

NOW, THEREFORE, BE IT FURTHER RESOLVED, that NCOIL urges Congress and the Administration to take action as soon as possible to extend that Program.

NAMIC®
NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

Statement

of

National Association of Mutual Insurance Companies

to the

United States Senate

Committee on Banking, Housing, and Urban Affairs

Hearing on

Reauthorizing TRIA: The State of the Terrorism Risk Insurance Market

September 25, 2013

Introduction

The National Association of Mutual Insurance Companies (NAMIC) is pleased to provide testimony on the Terrorism Risk Insurance Act (TRIA) and its vital role in helping protect our country and our economy as we continue to consider how to best handle the ever-present threat of terrorism.

NAMIC is the largest and most diverse property/casualty trade association in the country, with 1,400 regional and local mutual insurance member companies on main streets across America joining many of the country's largest national insurers who also call NAMIC their home. Member companies serve more than 135 million auto, home and business policyholders, writing in excess of $196 billion in annual premiums that account for 50 percent of the automobile/ homeowners market and 31 percent of the business insurance market. More than 200,000 people are employed by NAMIC member companies.

Since the events of September 11, 2001, the federal government has developed a robust and sophisticated counter-terrorism apparatus that has thus far succeeded in preventing large-scale terrorist attacks on the U.S. homeland. That said, the threat of terrorism is continuing to evolve amid a changing, unstable and dangerous international environment. Attacks such as the Boston Marathon bombings were a stark and painful reminder that the United States must remain vigilant. However unfortunate, it will likely never simply be about prevention – response and recovery are also integral pieces of national security apparatus. It is vital that we protect the U.S. economy from financial devastation and help get it back on its feet after an attack.

It is our firm belief that in the absence of a risk-sharing mechanism between the private and public sectors, no self-sustaining private market for terrorism risk coverage is likely to develop. However, the demonstrated success of the program has created the certainty needed for the commercial insurance industry to effectively operate and more importantly policyholders can purchase coverage that would otherwise be unavailable. Now, all but the largest terrorist attacks are completely borne by the private sector.

Some have characterized the program as another example of corporate welfare. A close examination of the facts reveals this characterization is not only false, but belies the very nature of the program. Indeed, the existence of TRIA *allows* a viable private market to function – rather than providing government assistance to commercial insurers.

It is important to remember that the response of the federal government to a large-scale terrorist attack – particularly in the absence of the risk-sharing mechanism – will not be inaction. The current TRIA program allows the insurance industry to completely cover losses for the far more likely smaller-scale attacks. This results in fewer uninsured losses meaning less government compensation after an attack. Without the program there will be more – not less – exposure to the taxpayers as the government will be under extreme pressure to pay for all or most of the losses. And TRIA does all this at no cost in the absence of an attack (except for negligible annual administrative costs) and with a built-in mechanism to recover every single penny the government pays out if there is a terrorist attack.

Therefore, we believe it is vitally important to our nation's finances, security, and economic strength that we maintain a long-term risk-sharing mechanism for terrorism insurance.

The TRIA Program – History and Structure

Before the events of 9/11, the abstract possibility of a major terrorist attack on the U.S. was known, but largely dismissed by most people. At the time, terrorism was typically included in "all-risk" policies because the risk was deemed so small as to be incalculable. In one morning, the 9/11 attacks caused roughly $40 billion in insured losses.

Soon after the events, reinsurers and then insurers moved to exclude terrorism coverage from their new and renewing policies as this was a poorly understood risk that could potentially produce unimaginable losses. Consequently, the ability of commercial policyholders to purchase adequate coverage at affordable prices was severely constrained. As a result, many were forced to go without coverage or only partly insure their assets. In states which prohibited carriers from excluding coverage for terrorism and with reinsurance companies universally excluding terrorist acts in property/casualty treaties, most carriers' only alternative was to offer less coverage or not write the business at all.

The lack of adequate insurance capacity and significant increases in pricing of commercial multi-peril business resulted in the postponement of many construction projects. It was estimated at the time to have delayed or cancelled $15.5[1] billion in real estate transactions and cost 300,000 construction workers their jobs.[2] Given the economic uncertainty that was created and the insurance industry's serious concern about properly managing this risk, Congress passed and President George W. Bush signed into law the Terrorism Risk Insurance Act of 2002. It was quickly realized that without the program American businesses would be hard pressed to find or afford the coverage they needed and so TRIA was extended for two years in 2005 and again in 2007 for seven years.

Essentially, TRIA placed a ceiling on individual company terrorism losses, which permitted them to quantify their terrorism exposure and make the coverage available..

[1] Real Estate Roundtable, "Survey Confirms Economic Toll of Terrorism Insurance Gap: Over $10 Billion of Real Estate Projects Affected Across U.S.," September 4, 2002.
[2] President George W. Bush, "President Reiterates Need for Terrorism Insurance Agreement," October 3, 2002.

The program was purposefully designed to force insurers back into a market, with the benefit of knowing their exposure.

Specifically, the program is a federal backstop for commercial property/casualty insurance that acts as reinsurance in the event of a certified terrorist event. A private insurance company pays for losses up to 20 percent of the prior year's direct earned premium on all lines of business covered in the TRIA program, which for the largest companies is several billion dollars, and then a 15 percent co-pay up to a program cap of $100 billion. After $100 billion, neither the government nor the company is required to pay for excess losses.

There are several other key elements to the program:

- **Program Trigger** – A terrorist event must hit a certain "trigger level" in order for there to be any Federal involvement. The trigger is currently set at $100 million.

- **Mandatory Offer** – The current program requires all insurers selling covered lines to offer terrorism coverage, compelling many insurers that had previously exited that market to return and dramatically reducing the amount of potentially uninsured losses in the event of an attack. Insurers are required to offer coverage for acts of terrorism on the same terms and conditions as other coverages, although this does not include coverage for nuclear, biological, chemical and radiological (NBCR) attacks. Currently policyholders are not required to purchase the offered coverage and in the last few years take-up rates have plateaued in the 60 percent to 65 percent ranges.

- **Recoupment** – Currently, *taxpayers are completely protected under TRIA* – the federal government has the ability to recoup any money that is spent through the program. By law the federal government *must* recoup the difference between insurers' total costs and the industry aggregate retention of $27.5 billion (assuming the total cost of the event with government payments is $27.5 billion or higher) over time through surcharges on every policy covered by TRIA. Since 2007, the government must actually recoup 133 percent of this mandatory recoupment. In the event the insurers' total costs exceed $27.5 billion then the government can still recoup whatever money it pays out, but this is at the discretion of the Treasury Secretary.

  In this way, the federal government can be thought of as a post-funded reinsurer for the catastrophic tail coverage of terrorism risks. This coverage is valuable, but not priced explicitly nor paid for upfront – it is paid for in the event it is used and in effect, pricing is determined after any event. It is common for risks that are more difficult to quantify and where there is great uncertainty as to the range of possible outcomes for benefits and policy limits to be determined up front and premiums after the policy period based on actual experience (nuclear power plant disasters are one example).

It is the structure of the current TRIA program that has created space for a private market to operate under the umbrella of federal participation. The private sector involvement reduces the unaddressed needs of victims which in turn reduces the necessity of government intervention – thus taxpayer exposure – post attack. Importantly, what TRIA does is define the government's role in advance of a catastrophe rather than relying on ad-hoc authorizations after the fact, thus allowing all parties to efficiently plan.

Why is the Program Necessary?

Managing terrorism risk defies the normal underwriting practices of insurers. Terrorism involves strategic human behavior and represents a dynamic threat that is intentional, responsive to countermeasures, and purposefully unpredictable. Immediately following 9/11, there was hope that, given time, more accurate modeling could be developed and utilized to help insurers manage the terror risk. And indeed, much has been done to develop tools to manage aggregate loss exposures that are based on a predetermined event of a certain magnitude in a given area.

That said, the underwriting challenges that remain are numerous and profound:

- Identical to Acts of War – Acts of war have always been considered uninsurable events with either an implicit or explicit expectation that financial responsibility resided with the governments involved. War-related damage has never been covered by insurers and no one has suggested that something must be done to maximize private sector capital to be used to provide such coverage. Simply because stateless, transnational groups are perpetrating these acts of terror does not categorically change them.

- Absence of Meaningful Actuarial Data – The data that insurers normally rely on when considering whether coverage can be offered and, if so, at what price, either does not exist or is not available. In the case of natural catastrophe risk, a company can rely on decades of relevant event data that can be plugged into mathematical models to quantify risk – there is no comparable historical record on which to draw for large-scale terrorist events. Further, much of the relevant data that might be used by an insurance company is appropriately kept secret by the federal government for national security reasons. Without access to this type of information insurers cannot meaningfully calculate the likelihood, nature, or extent of a potential event, making pricing and reserving virtually impossible. Although in theory access to classified information might paint a more accurate picture of the threat matrix facing targets in the U.S., insurers should not – and are not asking to – be given state secrets in order to write terrorism coverage.

- **Intentional Acts** – A related point is that terrorist acts are caused deliberately and do not occur randomly. Because of this, there is no way to determine the probability that a particular property or asset will experience a terrorism-related loss. Part of the difficulty in assessing terrorism risk stems from the fact that, because of response measures taken in the wake of an attack, the next event is unlikely to follow a similar pattern. Unlike criminal acts such as robbery where the goals are predictably targeted, the goal of maximizing death and destruction can be accomplished in countless ways, anywhere, and at any time. Terrorism is not comparable to a random event – a hurricane cannot study wind-damage mitigation efforts and then think up new ways to get around them. The only truly effective mitigation tools – if there are any -- reside within the government's national security apparatus, and as noted above, these are understandably kept secret.

- **Risk Concentration** – Terrorism risk is highly concentrated and incredibly difficult to effectively pool across geographical locations and policyholder type, particularly in an age of mass-casualty terror. Acts of terrorism on the scale of 9/11 are what are known as a "clash events" meaning they cause significant losses across multiple lines of insurance. These types of events directly threaten the solvency of both insurers and reinsurers and are not typically covered risks. In a fully free market, it would likely be the case that highly concentrated urban areas in particular would find it difficult to find or afford coverage for terrorism.

- **Interdependencies** – At the very highest level, the nation's foreign policy decisions and the effectiveness of its homeland defense have a direct impact on the likelihood and success of an attack. At the policyholder level, the vulnerability of one organization is not simply dependent on its own security decisions, but also on the decisions of other organizations and agents beyond its control.

In the end, it is more accurate to think of the TRIA program's purpose not as providing reinsurance for losses resulting from "acts of terrorism," but as protection against from losses that result from a failure in the government's systems for detecting and preventing acts of terrorism. With respect to natural catastrophe risk, it would be absurd to assign to a government agency the task of preventing hurricanes, tornadoes, and earthquakes. But it makes perfect sense for citizens to expect their government to prevent attacks by America's enemies, and that is precisely what Americans have come to expect from their government in the aftermath of 9/11. It is now widely recognized that one of the federal government's fundamental duties is to prevent terrorist attacks through the use of effective counter-terrorism measures. Only if the government does not fulfill its responsibility to protect Americans from terrorist attacks will Americans incur terrorism losses. "Terrorism risk" in 2013 and beyond is better understood as the risk of government counter-terrorism failure.

Accordingly, while the private insurance industry is willing to assume a substantial portion of this risk within the limits of its capability, the ultimate responsibility for managing the risk of government counter-terrorism failure does and should rest with the federal government itself.

What Would Happen if TRIA Expired or Was Materially Changed?

Termination of the program threatens the space in which a viable private market for terrorism insurance has grown. In considering what is likely to happen if the Terrorism Risk Insurance Program is terminated on December 31, 2014, the immediate aftermath of 9/11 in commercial property/casualty markets for terrorism coverage as described above is instructive.

Most insurers would likely not offer terrorism coverage in the absence of a federal risk-sharing mechanism like TRIA. To offer coverage for a risk that could result in a 9/11-size loss is a "bet the company" risk for insurers and they understandably withdrew from this segment of the market following 9/11. It was only with a program in place that put some structure around an ill-defined catastrophic risk that allowed insurers to participate. By providing more definitive loss parameters, TRIA has facilitated the participation of the private sector at current levels. We cannot hastily conclude that because the private sector can handle a portion of the risk, it could figure out a way to handle all of it.

Assuming that allowing the program to expire or drastically changing the federal government's role will simply result in private market innovation that has heretofore failed to materialize is unwise. State insurance regulators indicate that they have not seen evidence suggesting that the insurance marketplace is capable or willing to voluntarily take on a substantial portion of the risk of providing coverage for acts of terrorism in the absence of the program.

If TRIA is allowed to expire, it would create a particular disruption to worker's compensation system. Without a federal backstop, workers' compensation insurers will bear the entire financial burden of losses due to a terrorist attack. Reinsurers have shown an unwillingness to accept this potentially devastating risk or to offer affordable limits to protect the solvency of the workers' compensation insurers.

The workers' compensation benefit delivery system operates very differently from other property casualty insurance and should be given special attention in the debate to extend the program. Workers' compensation insurers are not allowed to exclude losses due to terrorism. The expiration of TRIA could result in disaster for workers' compensation insurers, and the businesses they serve, should a catastrophic terrorist event, occur. A migration of business currently being offered by private workers' compensation carriers to public state funds, residual markets and guaranty funds for large segments of metropolitan areas would be expected. These public options for workers' compensation are not designed to handle a catastrophic terrorist event. Injured workers and their families would face potential disruption in benefits. If the workers' compensation system fails, taxpayers could still be responsible for compensating victims – the very scenario that some policymakers want to avoid by letting TRIA expire. There would be delays in payment and hardship for those injured because of the lack of an efficient compensation system. These disruptions can be averted. Extending TRIA is more than a federal backstop for insurers – it is a social and economic imperative.

The effects of a termination of the TRIA program extend beyond the property/casualty insurance industry. As we saw, commercial development can grind to a halt in the absence of terrorism coverage if the financial institutions financing projects require the coverage as a condition of their loans. In fact, many outstanding loans that require developers to maintain coverage would be thrown into technical default if the program were terminated and insurers had made arrangements to exclude or limit coverage in the absence of TRIA. The impact on the broader economy was one of the key reasons that the program was first put into place and why it has continued to be reauthorized and nothing has fundamentally altered this dynamic.

A more pedestrian point involves the fact that private insurance companies, including mutual companies, are return-seeking operations. Therefore, if they believe there is an opportunity to earn an economic return and it is possible to do so in accordance with an overall successful business model, then they will. In other words, if there was money to be made in insuring against terrorism risk, coverage would be offered without government intervention. To that point, the companies would be arguing for less—not more—government intervention to increase that earning potential. The fact that they are uniformly not doing so and in fact suggesting that without the TRIA program private coverage would not expand and instead retract, is telling.

In seeking to accomplish the goal of increasing private sector participation in the terrorism insurance market, it is important to recognize that the entire marketplace as it stands today has grown up in the presence of the TRIA program. Insurance industry capital remains insufficient to absorb the cost of a large-scale terrorist attack on its own – simply put, the insurance industry's capacity is dwarfed for most modeled long-tail, high severity, catastrophic terrorism events. That capacity cannot be exposed beyond a reasonable level without failing in its primary purpose - supporting the economy by protecting against non-terrorism related losses and events. In the event of a major attack, substantially depleted reserves and surpluses, and insolvencies could mean that policyholders of non-covered lines could go unprotected. A company that engages in business that endangers the ability to pay on existing or future policies is violating its duties to existing policyholders.

Moreover, even if the overall industry capacity was significantly greater, serious concern about terrorism risk would remain for individual insurance companies. For a catastrophic event, the losses are not likely to be spread evenly among a large number of insurers. Thus terrorism risk is a situation in which no firm will be the "average" company. Insurance companies may either suffer no losses or else they could suffer losses sufficient to threaten their very existence. This dynamic lends itself to very strict underwriting and would severely constrain the private market in the absence of TRIA.

NAMIC would also caution policymakers not to assume that they can increase private sector participation by fiat. Increasing the nominal amount of private sector involvement in the current TRIA structure does not immediately translate into an increase in private sector capital in the marketplace. In fact, altering trigger levels or individual company retentions may cause market participants – particularly small and medium-sized companies – to exit, thereby reducing total private capital. An effective public-private partnership also depends on participation by insurers of all sizes and structures.

It is not at all clear that eliminating or scaling-back the TRIA program would lead to more involvement in the market by private insurers. In fact the opposite is likely true.

Improving the Program

The current TRIA program has worked very well. In large part this is because it has provided some certainty and predictability to a difficult risk. That said, NAMIC has suggestions to help improve the operation of TRIA in the event of an attack.

- Streamlining Functionality of Program – The TRIA program is capped at $100 billion dollars, a level above which neither the insurance companies nor the federal government is responsible for further payment. What is not clear is how proration would work for either the insurers or the policyholders. Which companies get to stop paying when, and which policyholders have to take how many cents on the dollar remains unclear. Providing clear guidance on how an event of this magnitude would work would provide more certainty for market participants.

- Certification of Terrorist Event – Although the Boston Marathon bombing did not come close to losses that would have hit the $100 million trigger, the debate surrounding certifying the event as a terrorist attack, which ultimately led to no certification, has led to significant concern in the industry. Insurance contracts are written and priced with specific terms and exclusions in mind and to the extent that a Treasury certification can become an uncertain political process that impacts a company's claims, it sets a bad precedent. To continue to encourage insurers to write covered TRIA lines – or to write any lines in markets perceived to have a higher terrorism risk – strengthening the predictability of the certification process, including imposing a deadline for certification, should be a part of the reauthorization process.

Conclusion

Since the passage of TRIA in 2002, the U.S. has been fortunate not to have suffered another event like 9/11. Therefore the program has not demonstrated its ability to help the nation recover in the aftermath of such a disaster. What we can and have seen is the market that has formed in the space created by the program, almost certainly drawing in more private capital than had the program been structured differently. TRIA was able to accomplish this without paying out a dime to the private sector and without creating a new fund or revenue stream or bureaucratic structure, all while creating a system that will reduce taxpayer exposure in the event of a massive terrorist attack.

In the end, the purpose of the program is not to protect insurers, but to make sure that the economy can recover in as orderly a fashion as possible from a terrorist event. In order to encourage private sector involvement in the terrorism insurance marketplace – and thereby protect and promote our nation's finances, security, and economic strength – we must maintain a long-term private/public partnership for terrorism risk insurance.

NAIC National Association of Insurance Commissioners & The CENTER for INSURANCE POLICY and RESEARCH

September 25, 2013

The Honorable Tim Johnson
Chairman
U.S. Senate Committee on Banking,
Housing, and Urban Affairs

The Honorable Michael Crapo
Ranking Member
U.S. Senate Committee on Banking,
Housing, and Urban Affairs

RE: Terrorism Risk Insurance Act

Dear Chairman Johnson and Ranking Member Crapo:

Thank you for holding this hearing to examine issues regarding the Terrorism Risk Insurance Act (TRIA). On behalf of the National Association Insurance Commissioners (NAIC)[1], we write today to express our support for TRIA reauthorization and to urge prompt Congressional action to renew this important partnership between the private insurance market and the federal government.

As you gather information and consider reauthorizing TRIA, we would like to submit for the record our resolution in support of TRIA reauthorization and our comment letter to the President's Working Group on Financial Markets.

We look forward to working with you as you continue to discuss TRIA reauthorization and would encourage all Members of Congress to discuss the program with your state's insurance commissioner. Should you have any questions or wish to discuss our comments or any other matter relating to the NAIC's views on this issue, please do not hesitate to contact Brooke Stringer, Financial Policy and Legislative Advisor, at (202) 471-3974.

Sincerely,

James J. Donelon
NAIC President
Louisiana Insurance Commissioner

Adam Hamm
NAIC President-Elect
North Dakota Insurance Commissioner

Monica J. Lindeen
NAIC Vice President
Montana Commissioner of Securities & Insurance

Michael F. Consedine
NAIC Secretary-Treasurer
Pennsylvania Insurance Commissioner

Enclosures
cc: The Honorable Jon Tester, U.S. Senate
The Honorable Mike Johanns, U.S. Senate

[1] Founded in 1871, the NAIC is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and the five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

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National Association of Insurance Commissioners (NAIC)
Resolution to Support Reauthorization of the Terrorism Risk Insurance Act

Adopted August 26, 2013

RESOLUTION

WHEREAS, the Terrorism Risk Insurance Act of 2002 (TRIA) was adopted and subsequently reauthorized twice by Congress to provide a federal shared loss program for incurred losses resulting from certain acts of terrorism in order to protect American businesses by minimizing market disruptions and ensuring the widespread availability and affordability of property and casualty insurance for terrorism risks;

WHEREAS, state insurance regulators have supported TRIA since its inception and its subsequent reauthorizations in 2005 and 2007; and

WHEREAS, the presence of the federal backstop has provided a measure of security to the insurance industry and has enabled insurers to extend offers of coverage for acts of terrorism following the tragic events of September 11th; and

WHEREAS, to date, state insurance regulators have not seen evidence suggesting that the insurance marketplace is capable or willing to voluntarily take on a substantial portion of the risk of providing coverage for acts of terrorism; and

WHEREAS, the evidence state insurance regulators have seen suggests that unknown frequency, coupled with the potential for substantial severity of a loss makes coverage for acts of terrorism one that insurers would likely choose to avoid if given the opportunity.

NOW, THEREFORE BE IT RESOLVED THAT:

State insurance regulators support the reauthorization of TRIA to help ensure market stability through the availability of terrorism coverage and urge prompt Congressional action prior to the program's expiration at the end of 2014 in order to minimize disruptions to the commercial insurance markets.

NAIC National Association of Insurance Commissioners & The Center for Insurance Policy and Research

September 16, 2013

Michael T. McRaith
Director, Federal Insurance Office
Room 1319 MT
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

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

Dear Director McRaith:

We write on behalf of the National Association of Insurance Commissioners (NAIC) to offer comments regarding the President's Working Group on Financial Markets' analysis of terrorism risk insurance. Founded in 1871, the NAIC is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and the five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer reviews, and coordinate their regulatory oversight. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

State insurance regulators have supported the Terrorism Risk Insurance Act (TRIA) since its inception and its subsequent reauthorizations, and the NAIC recently adopted a resolution reiterating its strong support for continuation of the program. We believe that the presence of a federal partnership with the private insurance markets has provided a measure of security to the insurance industry by minimizing market disruptions and ensuring the widespread availability and affordability of property and casualty insurance for terrorism risks. The availability of this coverage provides stability to commercial policyholders, lenders, builders, and the businesses that operate in urban centers and other areas prone to a terrorist attack. This public-private partnership ensures that insurers bear primary financial responsibility for losses from terrorism and must make the coverage available, while effectively capping the magnitude of losses and recouping federal funds if they are expended.

State insurance regulators have not seen evidence to suggest that the insurance marketplace is capable or willing to voluntarily take on a substantial portion of the risk of providing terrorism risk coverage. The difficulty in accurately determining the frequency, severity, and loss costs for acts of terrorism makes coverage for acts of terrorism one that insurers would likely choose to avoid if given the opportunity. If TRIA were allowed to expire, some insurers might place limitations on commercial insurance policies to exclude terrorism coverage or choose to withdraw from the market completely. While a permanent solution to terrorism risk insurance would be ideal, we support a prompt, long-term reauthorization of TRIA to help ensure economic stability through the availability of terrorism coverage.

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Attached to this letter are the NAIC's responses to the questions posed in the Federal Register. The NAIC and its Terrorism Insurance Implementation Working Group look forward to a continued dialogue with the Department of the Treasury regarding long-term solutions to address the risk of loss from acts of terrorism. Should you have any questions regarding these comments please do not hesitate to contact Eric Nordman, Director of the Regulatory Services Division and Director of the Center for Insurance Policy and Research, at (816) 783-8005 or Brooke Stringer, Financial Policy and Legislative Advisor, at (202) 471-3974.

Sincerely,

James J. Donelon
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NAIC Vice President
Montana Commissioner of Securities & Insurance

Michael F. Consedine
NAIC Secretary-Treasurer
Pennsylvania Insurance Commissioner

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

TRIA Termination Considerations

(1) Describe and explain in detail any and all possible ramifications from the termination of the Program on December 31, 2014, including any available evidence to support the predicted result, regarding: (a) The availability and affordability of insurance for terrorism risk in the United States generally;

To reduce the cost and increase availability of coverage for acts of terrorism, insurers need to be able to accurately estimate their ultimate expected loss costs associated with the risk transfer and related costs of capital. To do so requires knowledge of both the expected frequency and severity of future losses. In the case of coverage for acts of terrorism, severity and to a greater degree frequency, are extremely difficult to predict. When insurers are unable to determine what price to charge, they understandably tend to restrict coverage. This problem is partially resolved through the Terrorism Risk Insurance Act (TRIA) by providing insurers with a cap on the severity of exposures. With limitations in place, insurers can more reasonably assign a price to coverage that will not threaten their solvency and will place them in a better position to make such coverage available.

Unfortunately, there is no empirical measure of availability and affordability since they are both subjective measures and intertwined concepts in most cases. It can be argued that coverage for every peril is available to anyone if they are willing to pay any price. However, as a practical matter, if businesses perceive that coverage for acts of terrorism is too expensive for the risk of loss presented, they will choose not to buy the coverage. Further, if insurers perceive that not enough is known about the frequency or severity of losses caused by acts of terrorism, they will choose not to make the coverage available, unless either the state or federal government forces them to do so. If TRIA is not reauthorized, the absence of a federal backstop may lead insurers to choose to withdraw from the market completely.

Insurance regulators generally agree termination of TRIA would result in an availability crisis as insurers would not voluntarily offer coverage for acts of terrorism to most U.S. businesses. Evidence for this comes from the fact that, in the past, the insurance industry has filed conditional exclusions[1] in all states, and has received approval to use them in all but two states. It is possible a limited market for terrorism coverage would develop; however, regulators expect the cost would be high and the coverage very limited in scope.

(b) The availability and affordability of insurance for terrorism risk in the United States specifically by line of business; geographic location, including the rating tiers defined by the Insurance Services Office, Inc.; and other relevant characteristics;

The availability and affordability of terrorism insurance suffers in areas often referred to as Tier 1 terror targets, i.e., those that due to their size, location and potential impact on the economy as a whole are primary targets for terrorist groups. Terrorists seek to inflict maximum loss,

[1] Conditional exclusions for terrorism are policy endorsements that add terrorist events to the standard war and military action exclusions, in the event the TRIA program is either not reauthorized or undergoes major changes. These exclusion endorsements typically apply to commercial property and liability insurance policies, and to personal lines property insurance in states that have not enacted the New York standard fire policy.

resulting in no limit to the scale of property or casualty loss. Principal U.S. cities such as New York, Boston, Washington, D.C., Chicago, Miami, Houston, San Francisco and Los Angeles are the primary focus of terrorism, making these risks highly concentrated. This leads to adverse selection as the strongest demand for terrorism insurance originates in these geographic areas. If TRIA is not extended, state regulators believe terrorism insurance would become less available and affordable in the areas with the most need for coverage. We also believe that the elimination of the program may negatively impact the availability of insurance in mid-size cities and some types of commercial enterprises as well.

Workers' compensation coverage is a special case since terrorism cannot be excluded from individual workers' compensation policies. An expiration of TRIA would be especially disruptive to the workers' compensation market. It is likely that the size of residual markets would grow. In particular, businesses with large numbers of employees concentrated in a single location would be vulnerable as would businesses located near iconic buildings perceived to be attractive targets for terrorists.

(c) Additional specific effects on commerce in the United States.

As stated above, state regulators believe the expiration of TRIA would lead to terrorism insurance becoming unavailable and unaffordable as the insurance marketplace is not willing to voluntarily take on the risk of providing coverage for acts of terrorism. Insurers are not willing to jeopardize their financial health by accepting the potential unlimited severity and unpredictable frequency. This would lead to many businesses not having proper terrorism risk coverage, leaving them vulnerable to terrorism acts. In the absence of reauthorization, many businesses could not get proper coverage. During past debate over reauthorization of TRIA, regulators report receiving numerous inquiries from policyholders about not being able to obtain construction loans from banks. A slowdown in lending would have a chilling impact on the economy as mortgage lending and securitization of mortgage loans provides a significant portion of the GDP. One rating agency has said it may decline to rate commercial mortgage backed securities on transactions that lack sufficient terrorism insurance.

Insurance regulators in the Northeast have been involved with the rebuilding of infrastructure and communities after the destruction of Superstorm Sandy and they are particularly concerned that the expiration of TRIA would severely harm the rebuilding efforts. Further, building owners in Tier 1 & 2 areas might have difficulty attracting tenants as they might be unable to obtain coverage on the building and the tenants might be unable to obtain coverage on business operations and workers' compensation covering their employees.

Rating agencies have publicly stated they are seeking detailed plans from insurers in the event that the Program is not renewed due to rating concerns over the availability and affordability of terrorism coverage in the absence of a federal backstop. Insurers without a sufficient plan of action to handle terrorism risks may face rating downgrades as the expiration date approaches.

(2) If the Program were to continue beyond December 31, 2014, describe and explain in detail any revisions or modifications to the Program that would promote the availability and affordability of terrorism insurance, including any accompanying challenges that might arise from any proposed revisions or modifications to the Program. All views regarding the appropriate role of the federal government in supporting the availability and affordability of insurance for terrorism risk are welcome.

State insurance regulators encourage the development of a permanent solution to terrorism risk insurance in order to avoid the market disruptions and uncertainty associated with continual short-term reauthorizations. While ideally we would support a permanent solution, we recommend a prompt, ten-year TRIA reauthorization.

State insurance regulators believe that reauthorization of the Program is needed to provide a measure of security in the insurance industry and to enable insurers to extend offers of coverage for acts of terrorism. Regulators have particular concern with the timing of any revisions or modifications to the Program. A delay in the reauthorization of the Program creates uncertainty and deprives insurers of adequate time make necessary changes to systems, potentially leading to issues with policy renewals for policyholders. Regulators have already reported receiving filings that provide conditional exclusions in the event that the Program is revised or does not continue. These conditional filings apply to changes to deductibles, co-pays, limits and other changes in the Program. These exclusions create uncertainty in the marketplace with policyholders.

The commercial insurance business cycle operates in such a way that insurers and their policyholders will be required to make decisions as early as September 2013 for coverage going well into 2015. Annual policy renewals with effective dates of January 2, 2014, or later will have to contemplate no federal backstop for any losses in 2015. As a result, insurance regulators in most states are approving and will have to approve conditional coverage limitations for terrorism coverage for renewal policies on a widespread basis, just as they did in the 2006-2007 time period.

If triggered by the expiration of TRIA, these limitations would greatly reduce or eliminate terrorism coverage in the states that have approved the endorsement. In those states that have rejected these coverage limitations, insurers would have to make the difficult choice of writing the coverage and accepting the potentially catastrophic terrorism exposure or not writing the policy at all. This could lead to availability and affordability problems in the near future. With the 2014 renewal cycle already underway, there is greater uncertainty in the marketplace. For these reasons, insurance regulators encourage action by Congress this fall rather than waiting until 2014 to address the matter.

Insurance Market Considerations

(3) Describe and explain the ability of the insurance industry to model, quantify, and underwrite terrorism risk, and the resulting impact of such analysis on the availability and affordability of terrorism insurance, including an examination of the price (by line of business, location of risk, and other relevant characteristics) and coverage options for terrorism insurance.

Computer modeling of terrorism risk has been developed and refined by risk modelers since Sept. 11, 2001 in an attempt to measure an insurer's risk of loss from acts of terrorism. Many *insurers have begun to use the computer simulation models to assist them in pricing. While these models provide insurers with additional information about their risks and may provide more validity to premium rates in the future, the accuracy of models particularly with respect to frequency remains uncertain.*

While some computer simulation modeling has been introduced, the modeling efforts and their results are untested. The models are based on the opinions of counterintelligence experts along with assumptions regarding the type of damage that would occur if certain weapons were deployed. Insurers have relied upon them because they have no other choice. Insurers continue to express reservations about their ability to measure the risk of loss from acts of terrorism largely because even though modeling might be able to estimate the severity of loss resulting from specific terrorist events, there is no way to determine the frequency of such events. Unlike weather events or seismic events, which are outside human control and which occur with some statistical regularity, terrorist events are solely dependent on the will of those who seek to carry them out and the effectiveness of those who seek to prevent them. Thus, the insurance industry is left with very little on which to base frequency, and even the most sophisticated terrorism models amount to little more than educated guesses.

A recent presentation by a catastrophe modeler before the NAIC Property and Casualty Insurance Committee gave regulators insight into current modeling developments. An interesting comment from the modeler was that the TRIP was needed because insurers are essentially agreeing to provide coverage for government's failure to protect its citizens from terrorist acts. The modelers have learned that the more individuals there are involved in plotting a terrorist act, the more likely they are to be caught through governmental anti-terrorism efforts. They remain uncomfortable with their ability to model the severity of terrorism losses or the frequency. The frequency is dependent on the success of government anti-terrorism activities and the severity is boundless, according to the modeler.

(4) Describe and explain, with supporting information where available, any additional insurance market considerations that could impact the long-term availability and affordability of terrorism insurance (*e.g.* implications for coverage of insurance for nuclear, biological, chemical, and radiological acts of terrorism; cyber acts of terrorism; and terrorism in workers' compensation policies).

The magnitude of potential terrorism risks, for example, those from nuclear, biological, chemical, and radiological (NBCR) losses, is so great that it does not conform to the traditional methods available to insurers to spread and share the risk. Industry representatives consider the limited amount of capital available to insure all commercial losses to be inadequate to cover a large-scale NBCR event. An NBCR event has the potential to affect a large geographic area. This creates a large potential concentration of risk that may have substantial implications for individual insurers. Even with TRIA's loss limitations, the potential of a severe event may dissuade insurers from providing the coverage given their exposure to TRIA's deductible and co-insurance requirements.

Preliminarily, the NAIC would like to provide a general overview of NBCR coverages with the caveat that, as is the case with all causes of loss, coverage for any specific claim will ultimately be governed by the policy provisions, conditions and exclusions of the policy under which the claim is made.

Generally speaking, there is no coverage for nuclear or radiological incidents, terrorist-related or otherwise, because policies contain nuclear and radiological exclusions. This is true even in situations where the insured has purchased TRIA terrorism coverage. A terrorist event involving a nuclear/radiological device would not result in coverage because TRIA terrorism coverage only applies to covered perils under the policy and a nuclear event is not a covered peril. However, in states that mandate use of the New York Standard Fire Policy, and regardless of whether the insured has purchased TRIA terrorism coverage, fire losses following any nuclear event will be covered subject to other policy conditions and requirements. Also, it should be noted that the Price-Anderson Act establishes an insurance mechanism to provide insurance to operators of nuclear reactors in the U.S. in the event of a nuclear accident.

Standard policies generally do not contain a specific exclusion for losses from chemical or biological weapons. However, many policy forms include pollution or contaminant exclusions. Depending on the specifics of the incident in question, these exclusions might eliminate coverage from the policy for chemical or biological events. TRIA terrorism coverage for chemical or biological events would apply, if such events were considered covered perils under the primary policy. As noted above, in states that mandate use of the New York Standard Fire Policy, and regardless of whether the insured has purchased TRIA terrorism coverage, fire following a chemical or biological event will be covered subject to other policy conditions and requirements.

Finally, it is important to note that workers' compensation policies do not permit exclusions for NBCR events.

To the extent that coverage for NBCR events exists in primary policies, as explained above, insurers are required to make it available pursuant to TRIA for certified acts of terrorism. Specific information regarding the affordability of this coverage is not available to the NAIC at this time. Since the policy forms either include or exclude coverage for NBCR events without distinction as to the cause of the event, there should be no difference in the availability of coverage for such events caused by acts of terrorism. Affordability may be impacted to the extent that insurers will consider their exposure to terrorist acts and will ultimately reflect this exposure in the additional premium charged for TRIP coverage.

There is a report by the Government Accountability Office (GAO) on the topic of NBCR coverage (GAO-09-39). The findings in the report are as accurate today as they were when the report was written. The GAO found insurers generally seek to exclude coverage for NBCR events in commercial policies, relying on long-standing standard policy exclusions for nuclear and pollution risks. Further, the GAO found insurers "generally remain unwilling to offer NBCR coverage because of uncertainties about the risk and the potential for catastrophic losses..." Regulators believe these findings accurately describe today's marketplace.

Most standard commercial lines policies do not cover cyber risk. To cover these unique cyber risks through insurance requires the purchase of a special cyber liability policy. The markets for these policies are relatively new with a growing number of insurers offering coverage. Like all new markets, coverage contained in the policy forms is evolving as risks evolve and competitive forces come into play. There are some risks that are commonly covered by cyber liability policies. Generally cyber liability policies cover a business' obligation to protect the personal data of its customers. The data might include personal identifying information, financial or *health information or other critical data that if compromised could create a liability exposure for the business. The policy will cover liability for unauthorized access, theft or use of the data or software contained in a business' network or systems. Many policies also cover unintentional acts, errors, omission or mistakes by employees, unintentional spreading of a virus or malware, computer thefts or extortion attempts by hackers. At this time, insurance regulators do not believe it has been demonstrated that there is a need for acts of cyber terrorism to be included in TRIA.*

(5) Explain and describe in general the demand (or "take-up") of terrorism insurance and provide specific data and information, where available, regarding the take-up rate by line of business, location of the risk, and other relevant characteristics.

The insurance industry is best suited to address this issue.

Reinsurance Considerations

(6) Describe and explain in detail the long-term availability and affordability of private reinsurance for terrorism risk. Analyze, with supporting information, the impact of the Program, and any changes to the Program, on the private reinsurance market for terrorism risk, including any accompanying challenges that might arise from revisions or modifications to the Program.

The reinsurance industry is best suited to address this issue.

Additional Consideration

(8) Describe and explain any other developments, considerations, or market issues that might affect the long-term availability and affordability of terrorism risk insurance.

TRIA provides insurers with the security they need to allow them to offer coverage for acts of terrorism. It gives insurers a boundary on their ultimate costs of insuring the risk, and provides the maximum probable loss statistic for ratemaking and solvency purposes. It is important to note that TRIA requires the private insurance industry to cover losses up to $100 million, and only after that point would the federal government provide assistance. To date, this threshold has never been met and the federal government has never paid claims under TRIA. If the federal government were to pay claims under TRIA, there is a recoupment mechanism so, in most cases, losses paid for by the program would be reimbursed by a surcharge on property and casualty policies in future years. In our view, a permanent solution to insuring for terrorism risks would be ideal, but we urge a prompt, ten-year reauthorization of TRIA to avoid disruptions to the commercial insurance marketplace.

The Jewish Federations® OF NORTH AMERICA
Washington Office

THE **STRENGTH** OF A PEOPLE
THE **POWER** OF COMMUNITY

September 24, 2013

The Honorable Tim Johnson
Chairman
Committee on Banking, Housing, and Urban Affairs
United States Senate
Washington, DC 20510

The Honorable Mike Crapo
Ranking Member
Committee on Banking, Housing, and Urban Affairs
United State Senate
Washington, DC 20510

Dear Chairman Johnson and Ranking Member Crapo:

We commend the Committee for scheduling a hearing tomorrow on the extension of the Terrorism Risk Insurance Act (TRIA), which will expire in December 2014. On behalf of The Jewish Federations, I want to express our strong support for Congress renewing this legislation.

JFNA is the umbrella organization of 153 local federations and 300 independent communities which serve, support, and lead one of the Nation's largest and longest serving charitable networks that provide health, human services, and other critical humanitarian assistance at the community level. We are headquartered in New York City and our system's hospitals, nursing homes, social services agencies, and community centers are located in practically every major urban area in the United States.

Given the well documented threats from extremists at home and abroad to Jewish communal security, we believe that our institutions across the country represent a segment of the nonprofit sector that is particularly at risk of and vulnerable to terrorist attacks. (See threat overview document attached)

However, in surveying our institutions, we have found that TRIA has successfully ensured that the insurance market continues to make widely available to them adequate and affordable terrorism coverage since 9/11. Our system's catastrophic exposure has remained significantly reduced as a consequence of TRIA.

Our network serves tens of thousands of individuals and families in need, weekly. In times of disaster – whether in the recovery from Super Storm Sandy, Hurricane Katrina, or the attacks on September 11th, among them – our agencies help to rebuild communities through the provision of health care, counseling, shelter, resettlement, job training, food, family support services, and emergency cash assistance. We are often home-base to emergency responders for staging and coordination. TRIA has proven essential to our ability to carry out these vital services, both in the regular course of our work and in times of extenuating circumstances.

For these reasons, we urge the Committee to continue to support the Terrorism Risk Insurance Act and its renewal.

Sincerely,

Robert B. Goldberg
Senior Director, Legislative Affairs

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Washington, DC 20006-3736

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The Jewish Federations OF NORTH AMERICA

Risk Overview: Threats, Vulnerabilities and Potential Consequences
September 24, 2013

Existential Threats to Jewish Communal Institutions:

- Since 9/11, the FBI, Department of Homeland Security and other law enforcement entities have warned the U.S. Jewish community of a number of plots by international terrorist organizations, white supremacists, prison Islamic radicals and other homegrown violent individuals across the political spectrum. While a number of prominent plots have been averted, others became operationalized.

- One regular thread among many terrorist occurrences is the symmetrical selection of targets that include both government/military facilities/personnel, and Jewish communal institutions and civilians. One large distinction, however, is that the latter category comprises soft nonprofits with limited resources and capabilities with which to harden their facilities and to train their personnel.

- Additionally, over the past decade, the FBI has reported that approximately 70% of religious-based hate crimes have been perpetrated against the Jewish community – well above the combined occurrences of all other faiths.
  (Source: Annual FBI Hate Crimes Statistics Reports; Link:
  http://www.fbi.gov/news/stories/2012/december/annual-hate-crimes-report-released/annual-hate-crimes-report-released)

- **December 10, 2012:** Of the 1,480 victims of an anti-religious hate crime, 63.2 percent were victims of an offender's anti-Jewish bias – more than all other categories combined.
  (Source: FBI Hate Crime Statistics, 12/10/12; Link:
  http://www.fbi.gov/news/stories/2012/december/annual-hate-crimes-report-released/annual-hate-crimes-report-released)

- **July 20, 2012:** New York police believe Iranian Revolutionary Guards or their proxies have been involved so far this year in nine plots against Israeli or Jewish targets around the world. According to NYPD analysts, "through its own Revolutionary Guard and Hezbollah, Iran had "sharply increased its operational tempo and its willingness to conduct terrorist attacks targeting Israeli interests and the International Jewish community worldwide".

(Source: Reuters, 07/20/12; Link: http://www.reuters.com/article/2012/07/20/us-iran-hezbollah-plots-idUSBRE86J0SW20120720)

- June 5, 2012: According to Homeland Security Secretary Janet Napolitano, "Jews face special risks that require vigilance." She also stated that, during her tenure at DHS, threats to the Jewish community came from foreign entities, homegrown extremists and domestic hate groups.
(Source: The Forward, 06/05/12: Link: http://forward.com/articles/157280/jews-face-special-risks-napolitano-says/?p=all)

- February 16, 2012: With tensions between Iran and the West running high, law enforcement officials are concerned Iran or its surrogates could mount attacks against Jewish targets inside the United States.
(Source: CNN, 02/16/12; Link: http://www.cnn.com/2012/02/15/us/iran-fbi-warning/index.html?iref=allsearch)

- January 9, 2009: Terrorist analysts report that throughout the world, Jewish communities will be specifically at risk from several "fatwas" disseminated through Arab media and jihadist websites, including one instructing that "any Jew is a legitimate target that can be struck by Muslims."
(Source: European Strategic Intelligence and Security Center, 01/09/09)

- March 24, 2008: Al Qaeda's second in command, Ayman al-Zawahiri, released an audio tape on, which called upon al Qaeda followers and sympathizers to attack Jewish interests worldwide. The tape, part of a string of provocative statements by bin Laden and his senior cohorts, was regarded by counter terrorism experts as a new and bold escalation by al Qaeda to link the Middle East conflict with immediate and urgent violence in the West, including against Jewish targets in the United States.
(Source: Associated Press, 03/24/08)

- November 24, 2002: In a "Letter to America" Osama bin Laden released soon after the 9/11 attacks, to explain his reasoning and intent to justify the attacks, he wrote, "The creation and continuation of Israel is one of the greatest crimes, and you are the leaders of its criminals." "This is why the American people cannot be innocent of all the crimes committed by the Americans and Jews against us." The letter also made clear that, to bin Laden, civilian populations, as with governments, were acceptable (equivalent) targets for retaliation.
(Source: Guardian (UK), 11/24/02; Full text of the letter: http://www.guardian.co.uk/world/2002/nov/24/theobserver)

- June 3, 2002: Abdul Rahman Yasin, one of the terrorists in the first attack on the World Trade Center in 1993, revealed in a CBS 60 Minutes interview that the World Trade Center was not the terrorists' original target. Rather, they initially planned to blow up Jewish neighborhoods in Brooklyn. But after scouting Crown Heights and Williamsburg, they decided to target the World Trade Center, instead. The reasoning: rather than undertaking multiple small explosions in Jewish neighborhoods, they figured that one big explosion in the World Trade Center would kill mostly Jews who they believed made up a majority of the workforce there, according to Yasin's statements.
(Source: CBS News 06/02/02; Reuters, 06/03/02)

- **February 2, 2002:** Shortly after the 9/11 attacks, Al Qaeda's training manual was translated by the Associated Press, which included a directive to followers to attack Jewish communal organizations and institutions in every country Jews exist and to carry out the attacks in a manner designed to cause the most causalities. It specified community centers, hospitals, places of worship and wherever there are large gathering places of Jews.
  (Source: Associated Press, 02/02/02)

Recent Jewish Security Threats:

- **May 16, 2013:** A 22-year-old Moroccan man has been convicted and sentenced to five years and four months in jail for plotting a terror attack against a Milan synagogue. The man was arrested in March 2012 after police noted that the suspect had used a Google maps application to case security at the synagogue.
  (Source: The Associated Press, 05/16/13)

- **May 7, 2013:** Israeli airstrikes on Syrian missile stockpiles suspected to be destined for Hezbollah raise concern for retaliation against Jewish civilians. According to the Washington Post, "U.S. and Middle Eastern officials say any retaliation would probably come in a familiar form: attempted attacks by Hezbollah operatives on Israeli or Jewish civilian targets, perhaps far outside the Middle East."
  (Source: Washington Post, May 8, 2013; Link: http://www.washingtonpost.com/world/national-security/western-officials-fear-retaliation-for-israeli-airstrikes-in-syria/2013/05/07/2989f1a4-b72f-11e2-92f3-f291801936b8_print.html)

- **May 1, 2013:** Bomb threats were phoned in to two different Houston synagogues (Congregation Beth Israel and Congregation Or Ami), causing their schools to cancel classes, so that the FBI and Houston Police Department could search the institutions for explosives. When the buildings reopen, it was reported that they will require extra security personnel and police presence. April 8, 2013: Ruben Ubiles, 35, who the police say has more than 50 prior arrests, on charges including robbery, assault, and weapons and drug possession, was arrested for the hate-crime burning of a dozen Jewish doorway adornments in Williamsburg, Brooklyn, on Holocaust Remembrance Day. The ornaments, known as mezuzot, contain scrolls with Old Testament verses that are intended to bless and protect the home.
  (Source: New York Times, 04/10/13)

- **March 18, 2013:** French President Francois Hollande on Sunday paid tribute to the seven people who last year fell victim to terrorist Mohamed Merah, saying he remains committed to the fight against terrorism. A self-described Al-Qaeda sympathizer, 23-year-old Merah murdered Rabbi Jonathan Sandler, his sons Aryeh and Gavriel and Miriam Monsonego at a Jewish school, Otzar HaTorah, in Toulouse. Before that, he murdered three paratroopers.
  (Source: Arutz Sheva, 03/18/13: Link: http://www.israelnationalnews.com/News/News.aspx/166321)

- **March 17, 2013:** Marked the 21st anniversary of the March 17, 1992 terrorist attack that left 28 people dead and 240 wounded at the Israel Embassy in Buenos Aires. Two years later (July 1994), 85 members of the Argentine Jewish community were killed in an

attack on a community center. This was the deadliest terror attack in Argentina's history. In both cases, the attackers were never caught.
(Source: Arutz Sheva, 03/17/13; Link: http://www.israelnationalnews.com/News/News.aspx/166301)

- March 15, 2013: An Algerian man convicted of plotting to bomb synagogues was sentenced to 10 years imprisonment. According to New York City Police Commissioner Raymond Kelly, ""Ferhani posed a real threat to New York's Jewish community, eagerly purchasing a hand grenade, two guns and 150 rounds of ammunition from an undercover officer as part of Ferhani's stated intention to attack and then 'blow up a synagogue in Manhattan, and take out the whole entire building."
(Source: CNN, 03/15/13)

- January 30, 2013: A new policy paper from the Washington Institute for Near East Studies finds that Iran's elite Qods Force and Hezbollah militants pose a growing threat to the U.S., fueling worries that they increasingly have the ability and willingness to attack the U.S., and, in particular, Jewish targets. Among the most likely scenarios, stated the report, "an attack targeting a location affiliated with a Jewish community abroad", such as the report noted, the 1994 bombing of AMIA Jewish community center in Buenos Aires.
(Source WINES, January 30, 2013; Link:
http://www.washingtoninstitute.org/uploads/Documents/pubs/PolicyFocus123.pdf)

- January 23, 2013: The Congressional Research Service published a comprehensive analysis on the complex threat of American Jihadist Terrorism, including particular threats to Jewish communal security: 1) The 2005 plot by the group Jamiyyat Ul-Islam Is-Saheeh, to attack Jewish institutions, including synagogues, and military recruiting offices and military bases, which the report described as the "most prominent post-9/11 example of domestic violent jihadist activity inspired in prison;" 2) The 2009 Newburgh Four case, which involved a plot to trigger explosive in front of a synagogue and Jewish community center and to shoot down military aircraft; 3) The 2011 grenade plot by Ahmed Ferhani, an Algerian, and Mohamed Mamdouth, a naturalized US citizen from Morocco, who plotted to blow up prominent synagogues in New York City; and 4) The 2012 bombing plot by Amine El Khalifi, a Moroccan citizen living in the US on an expired B2 tourist visa, who targeted the US Capitol, a synagogue, and a restaurant that was frequented by US military personnel.
(Source: CRS, 01/23/13; Link: http://www.fas.org/sgp/crs/terror/R41416.pdf)

- January 16, 2013: The FBI warned the Detroit Jewish community of potential risks after discovering in the home of a known white supremacist and convicted murderer, Richard Schmidt, 18 firearms including assaults weapons, high-capacity magazines, and more than 40 thousand rounds of ammunition; Nazi paraphernalia; a "Jewish hit-list" of 500 Jewish owned businesses; and detailed information on the leadership of the Jewish Federation of Metropolitan Detroit and diagrams of the facility.
(Source: US Attorney, Ohio, 01/16/13; Link:
http://www.justice.gov/usao/ohn/news/2013/16janschmidt.html)

Historic Record of Threats:

- **December 4, 2012:** A man from Queens accused of plotting to blow up a synagogue in Manhattan ended on Tuesday when the man, Ahmed Ferhani, pleaded guilty to 10 charges, including conspiracy as a crime of terrorism and criminal possession of a weapon as a crime of terrorism. He was arrested immediately after making a down payment in exchange for a hand grenade, three semiautomatic pistols and 150 rounds of ammunition.
  (Source: New York Times, 12/04/12; Link: http://www.nytimes.com/2012/12/05/nyregion/ahmed-ferhani-pleads-guilty-in-plot-to-blow-up-synagogue.html**)**

- **July 20, 2012:** New York police believe **Iranian Revolutionary Guards** or their proxies have been involved so far this year in nine plots against Israeli or Jewish targets around the world. According to NYPD analysts, "through its own Revolutionary Guard and Hezbollah, Iran had "sharply increased its operational tempo and its willingness to conduct terrorist attacks targeting Israeli interests and the **International Jewish community worldwide**".
  (Source: Reuters, 07/20/12; Link: http://www.reuters.com/article/2012/07/20/us-iran-hezbollah-plots-idUSBRE86J0SW20120720**)**

- **June 22, 2012:** The FBI announced the 11.5 year sentence for American Jess Curtis Morton, aka Younus Abdullah Muhammed, for **running several Internet sites in the United States to solicit attacks and future threat against Jewish organizations** in the US. His co-conspirator lived in Fairfax, VA (less than 20 miles from Capitol Hill). The web sites Morton ran perpetuated al Qaeda produced propaganda and **included hit lists.**
  (Source: U.S. Attorney's Office/Eastern District of Virginia, 06/22/12; Link: http://www.fbi.gov/washingtondc/press-releases/2012/leader-of-revolution-muslim-sentenced-to-138-months-for-using-internet-to-solicit-murder-encourage-violent-extremism?utm_campaign=email-Immediate&utm_medium=email&utm_source=washington-press-releases&utm_content=108401**)**

- **June 20, 2012:** This week, the New York Post described a new "Crime Wave" against Brooklyn's Jewish community when it reported several synagogue thefts and anti-Semitic vandalism targeting synagogues and Jewish neighborhoods.
  (Source: New York Post, 06/20/12; Link: http://www.nypost.com/p/news/local/brooklyn/anti_jewish_crime_wave_GNiORau6jWlqBeqM7ugEBO; **Forward, 06/05/12; Link:** http://m.forward.com/articles/157280**)**

- **June 5, 2012: According to Homeland Security Secretary Janet Napolitano,** "Jews face special risks that require vigilance." She also stated that, during her tenure at DHS, threats to the Jewish community came from foreign entities, homegrown extremists and domestic hate groups.
  (Source: The Forward, 06/05/12: Link: http://forward.com/articles/157280/jews-face-special-risks-napolitano-says/?p=all**)**

- **May 3, 2012:** On the anniversary of the bin Laden raid, the US Government released a sampling of documents. Only one pertained to approving funding for terrorism – the approval of a request by a militant group to purchase and manufacture weapons, and to **support operationsagainst the Jewish community.**
  (Source: CNN, May 3, 2012; Link: http://edition.cnn.com/2012/05/03/world/osama-bin-laden-documents/index.html**)**

- April 23, 2012: Meanwhile, the US just placed a $10 million bounty on Hafeez Saeed, the leader of Lashkar-i-Taiba, an al Qaeda-affiliated militant group, and the mastermind behind the 2008 Mumbai, India massacre. A paramount objective of the massacre was an attack on that city's Jewish community center and the torture and murder of its Jewish civilians. Saeed remains at-large.
  (Source: Pro Publica, 04.03.12; Link: http://www.propublica.org/article/10-million-bounty-for-alleged-mumbai-plotter-ups-pressure-on-pakistan)

- March 26, 2012: The livery driver whose two-gun attack on a group of Hasidic students on the Brooklyn Bridge shocked the city 18 years ago has finally admitted that he targeted them because they were Jewish, The Post has learned. Rashid Baz was convicted in 1995 of murdering Yeshiva student Ari Halberstam, 16, and trying to kill more than a dozen others in a van with a hail of bullets he fired on a Manhattan approach to the bridge on March 1, 1994.
  (Source: New York Post, 03/26/2012; Link: http://www.nypost.com/p/news/local/killer_jews_my_target_gOgyDs9rPP92Z5irIUqK1H)

- March 26, 2012: According to the Associated Press this morning, French authorities are defending criticism that their counterterrorism authorities and laws failed in preventing an Islamic terrorist attack that killed paratroopers, Jewish children and a rabbi (teacher) in front of a Jewish school in Toulouse, France. The general reaction from Europol, and a growing chorus of other European terrorist authorities, is that homegrown extremists are hard to track and stop; combating individuals acting in isolation will be tough and problematic; and it will be hard for police to apprehend them before they attack.
  (Source: Associated Press, 03/26/12)

- February 17, 2012: The FBI announced the indictment of Amine El Khalifi, an illegal immigrant from Morocco, for attempting a suicide attack on the Capitol. According to the indictment, El Khalifi had first indicated his intention to blow up a Jewish civilian target -- a synagogue.
  (Sources: FBI WFO; Link: http://www.fbi.gov/washingtondc/press-releases/2012/virginia-man-accused-of-attempting-to-bomb-u.s.-capitol-in-suicide-attack?utm_campaign=email-Immediate&utm_medium=email&utm_source=washington-press-releases&utm_content=72268; Criminal Complaint Link: http://www.washingtonpost.com/wp-srv/world/documents/amine-el-khalifi-criminal-complaint.html)

- February 16, 2012: With tensions between Iran and the West running high, law enforcement officials are concerned Iran or its surrogates could mount attacks against Jewish targets inside the United States.
  (Source: CNN, 02/16/12; Link: http://www.cnn.com/2012/02/15/us/iran-fbi-warning/index.html?iref=allsearch)

- February 15, 2012: A statement by House Homeland Security Committee Chairman Peter King called attention to the "almost imminent threat posed by Hezbollah quite possibly to Jewish houses of worship and religious institutions."
  (Source: Hearing: An Examination of the President's FY 2013 Budget Request for the Department of Homeland Security; Link: http://homeland.house.gov/hearing/hearing-examination-presidents-fy-2013-budget-request-department-homeland-security)

- **February 14, 2012: With Iran allegedly striking out at Israeli citizens and Jewish targets around the world, Israeli and American security officials in the U.S. are on high alert.** According to Frank Cilluffo, director of the Homeland Security Policy Institute at George Washington University in D.C., the recent incidents in India, Georgia, Thailand and Azerbaijan have "all the hallmarks of a concerted campaign" that could extend to U.S. soil. As such, the NYPD has adjusted its counterterrorism posture to include increased presence in recent weeks at Israeli government facilities and synagogues. Furthermore, around the country, private security industry officials report numerous requests for Jewish institutional security.
  (Source: ABC News; Link: http://abcnews.go.com/Blotter/heightened-security-us-iran-threat/story?id=15592451)

- **February 14, 2012:** In a lead story, **the New York Times reported on the escalation of threats posed by Iran (and its proxies)** -- meaning violent actions taken against Jewish targets outside of the region. The article followed recent plots and attacks that have increased the concern of American Jewish leaders for the safety and security of Jewish community centers and synagogues within the United States, and the article reminds that an attack on the Mumbai Jewish community center led to the torture and death of a number of Jewish American civilians in 2008.
  (Source: New York Times, 02/14/12; Link: http://www.nytimes.com/2012/02/14/world/middleeast/israeli-embassy-officials-attacked-in-india-and-georgia.html?_r=2&ref=world&pagewanted=print)

- **February 14, 2012:** Convicted arsonist/bomber Omar Bulphred, 26, will serve his full seven-year prison term for hate crimes - including the **firebombing of a Jewish school for children and attempted bombing of a Jewish community center** - will remain behind bars for his entire sentence as he continues to pose a serious problem for Correctional Service Canada (CSC).While investigating the fires, police found letters in which Bulphred and an accomplice declared jihad and demanded the liberation of their "brothers" - a group of men arrested on terrorism charges in Toronto.
  (Source: The Gazette (Montreal); Link: http://www.montrealgazette.com/news/todays-paper/Hate+crime+convict+refused+early+release/6148040/story.html)

- **February 10, 2012:** Nine extremists who "were well advanced in their terrorist planning were convicted. "The men possessed almost every famous jihadi publication, including copies of Inspire, an English language internet magazine produced by Yemen-based extremist cleric Anwar al-Awlaki's group Al Qaida in the Arabian Peninsula." According to the prosecution, "These men were motivated to act as they did in large part by extreme jihadist propaganda circulated on the internet. Convicted for **planning a "Mumbai" style attack that included targeting the Jewish community**, one of the group's leaders and his brother, "were bugged claiming that fewer than 100,000 Jews died in the Holocaust and talking about how Hitler "had been on the same side as the Muslims" because he understood that "the Jews were dangerous".
  (Source: http://www.mirror.co.uk/news/uk-news/british-terror-gang-that-plotted-to-blow-680112)

- **February 9, 2012:** The leader of "Revolution Muslim" pleaded guilty to using the **Internet to solicit murder and encourage violent extremism against Jews.**
  (Source: The FBI; Link: http://www.fbi.gov/washingtondc/press-releases/2012/leader-of-revolution-muslim-pleads-guilty-to-using-internet-to-solicit-murder-and-encourage-violent-extremism?utm_campaign=email-Immediate&utm_medium=email&utm_source=washington-press-releases&utm_content=69655)

- February 1, 2012: Four defendants inspired by al-Qaeda have admitted planning to detonate bombs – Mumbai-style – at five symbolic sites including the U.S. Embassy, the Palace of Westminster (both well-fortified institutions), and two prominent rabbis from separate synagogues. The men reportedly admitted to being inspired by the preachings of the radical al-Qaeda extremist Yemeni American imam Anwar Al-Awlaki and to being in possession of two editions of al-Qaeda magazine Inspire for terrorist purposes.
(Source: BBC News, Link: http://www.bbc.co.uk/news/uk-16833032)

- January 25, 2012: A joint attack by Iran and Hezbollah against Jewish targets in Bangkok, Thailand, had been stopped, where the operative in custody reportedly confessed to having intended to blow up a synagogue and the Israeli Embassy. Moreover, the New York Times story reported that Iran and Hezbollah have also planted some 40 terrorist sleeper cells around the world, ready to attack Jewish targets if Iran deems it necessary to retaliate against efforts to thwart its nuclear ambitions.
(Source: The New York Times Magazine, 01/25/12; Link:
http://www.nytimes.com/2012/01/29/magazine/will-israel-attack-iran.html?scp=1&sq=six%20key%20strikes%20thought%20to%20be%20made%20by%20the%20mossad&st=cse)

- January 13, 2012: Federal elected officials from North Jersey and across the state pledged resources in the investigation into the firebombing of a Rutherford synagogue at a meeting convened to discuss safety at Jewish temples Thursday night.
(Source: New Jersey On-Line; Link:
http://www.nj.com/bergen/index.ssf/2012/01/officials_pledge_federal_resources_for_investigation_into_temple_firebombing_bias_crimes.html)

- December 2, 2011: Homeland Security Director Janet Napolitano and Attorney General Eric Holder met with their counterparts from Britain and other European partners to discuss issues of points of cooperation in fighting terrorism. In seeking this meeting to improve the U.S.-EU partnership to combat global terrorism, the Secretary pointed to the success of shared efforts in aiding the investigation and prosecution of American David Headley, the mastermind behind the deadly attack on the Mumbai Jewish Community Center just over 3 three years ago – November 27, 2008.
(Sources: Associated Press; Link: http://www.cbsnews.com/8301-201_162-57336080/napolitano-lone-wolf-terror-threat-growing/)

- December 2, 2011: Jubair Ahmad, 24, a native of Pakistan and resident of Woodbridge, Va., pleaded guilty of providing material support to Lashkar-e-Tayyiba (LeT), a designated foreign terrorist organization. "By preparing and posting a graphic video that glorified violent extremism, Mr. Ahmad directly supported the mission of a designated terrorist organization," said FBI Assistant Director in Charge McJunkin. "The FBI will track down and disrupt those who communicate with terrorist groups for the purpose of recruiting others to inflict harm on the U.S. and its interests overseas." Ahmad considered including images of the Mumbai attack to show the power of LeT. This is a reference to LeT's operation against the city of Mumbai, India, on Nov. 26, 2008, which resulted in the death of over 160 people, including a number of Jewish Americans killed at the targeted Jewish Community Center.
(Source: U.S. Attorney, Eastern District of Virginia; Link: http://www.fbi.gov/washingtondc/press-

releases/2011/virginia-man-pleads-guilty-to-providing-material-support-to-terrorist-organization?utm_campaign=email-Immediate&utm_medium=email&utm_source=washington-press-releases&utm_content=53207)

- November 14, 2011: The FBI released hate crimes data for 2010. As has been the case since the FBI first began reporting incidents of hate crimes, approximately 70% of all religious bias crimes are committed against Jewish institutions and civilians in the US. (Source: FBI Hate Crime Statistics: http://www.fbi.gov/about-us/cjis/ucr/hate-crime/2010)

- November 9, 2011: The Cold War's most notorious international terrorists, Ilich Ramirez Sanchez (aka "Carlos the Jackel"), went on trial in France, on charges of instigating four attacks in 1982 and 1983. Sanchez's first terrorist strike was an assassination attempt against major British philanthropist of Jewish charities, Joseph Sieff. Sanchez gained entrance into Sieff's home by gunpoint, and shot the past vice-president of the British Zionist Federation at point blank range in the face.
(Sources: Associated Press; Link: http://m.ctv.ca/topstories/20111107/carlos-ilich-ramirez-sanchez-jackal-terror-trial-france-111107.html and TruTV; Link: http://www.trutv.com/library/crime/terrorists_spies/terrorists/jackal/1.html)

- January 17, 2011: Five synagogues and a Jewish school in a Jewish enclave in Montreal were attacked in a single night. Condemning the attack, the Liberal Leader, Michael Ignatieff, remarked, "Our thoughts and prayers are with Jewish communities across Canada that once again have been made to feel that their congregations and the children in their schools have cause to fear for their safety."
(Sources: The Globe and Mail (Canada), 01/17/11)

- October 29, 2010: Al-Qaeda in the Arabian Peninsula attempted to ship air cargo bombs addressed to Chicago-based synagogues.
(Source: MSNBC, 10/29/10)

- January 20, 2010: FBI Director Robert Mueller testified before the Senate Committee on the Judiciary that al Qaeda; self-directed groups linked to terror organizations; and self-radicalizing, self-executing homegrown terrorists remained determined to strike the country and the threat has not diminished.
(Source: http://judiciary.senate.gov/pdf/10-01-20Mueller'sTestimony.pdf, 01/20/10)

- December 28, 1009: The FBI Year in Review chronicled the U.S. top terror cases, including: the arrest of David Coleman Headley, a U.S. citizen, for his role in planning the 2008 Mumbai attacks, where six Americans (4 Jewish) were killed; the arrest of four radicalized individuals for attempting to blowup a Riverdale, New York synagogue and Jewish community center; the deadly shooting at the Holocaust Museum in Washington, DC; and the attack on an Army recruiting center in Little Rock, Arkansas, by an assailant who was also found to be targeting Jewish sites in Little Rock, Philadelphia, Atlanta, New York, Louisville and Memphis.
(Source: FBI Release, 12/28/09; Link: http://www.fbi.gov/page2/dec09/review_122809.html)

- December 15, 2009: the House Homeland Security Subcommittee on Intelligence, Information Sharing and Terrorism Risk held a hearing on the emergence of violent extremism and domestic terrorism in the U.S. In her opening remarks, Chairwomen Jane Harman (D-CA) focused on two infamous plots and attacks against Jewish

communal interests at home and abroad: 1) The plot by Jami'yyat Ul-Islam Is-Shaheeh, a prison-founded radical Muslim group, to attack prominent synagogues and other Jewish iconic sites in the Los Angeles area; and 2) The massacre in Mumbai, India, where American David Headley is now accused by federal law enforcement officials of having helped to identify and surveil for attack, among others, the Chabad House Jewish community center, whose director, Rabbi Gavriel Noach Holtzberg, his wife, unborn child, and four others were tortured and killed.
(Source: House Homeland Security Subcommittee on Intelligence, Information Sharing and Terrorism Risk, 12/15/09; Link: http://homeland.house.gov/Hearings/index.asp?ID=229)

- **September 13, 2009:** Osama bin Laden warned the American people over their government's close ties with Israel. In the tape, bin Laden warned, "If you stop the war, then fine. Otherwise we will have no choice but to continue our war of attrition on every front."
(Source: Washington Post, 09/13/09)

- **August 17, 2009:** A man was sentenced to 70 months in prison today for his role in a domestic terrorism plot to wage war on the United States by attacking Jewish synagogues and military bases. Hammad Riaz Samana is the fourth member of Jami'yyat Ul-Islam Is-Shaheeh, or JIS, a prison-founded radical Muslim group that wanted to make a political statement that also had plans to attack the Israeli consulate in Los Angeles and El Al Israel Airlines at the Los Angeles International Airport.
(Source: The Orange County Register, 08/17/09)

- **June 16, 2009:** Critical aspects of the nonprofit sector are particularly vulnerable and regular targets of terrorist groups and radicalized homegrown individuals. A number of incidents make this point clear. In remarking on the June 10, 2009, attack at the U.S. Holocaust Memorial Museum by a radical rightwing fanatic, Secretary Napolitano stated that the attack underscored the need for the Nonprofit Security Grant Program, so that high risk nonprofits can take their own security measures.
(Sources: Remarks by Secretary Napolitano Announcing Fiscal Year 2009 FEMA Preparedness Grants, Release, 06/16/09)

- **June 3, 2009:** The Arkansas man convicted of killing an Army recruiter and wounding another had used the popular Google Maps application to investigate recruiting centers in at least five states, as well as Jewish institutions in Little Rock, Philadelphia, Atlanta, New York, Louisville and Memphis.
(Source: ABC News, 06/03/09)

- **April 7, 2009:** Two accusatory tactics associated with the current rise in rightwing radicalization and the potential for violence are aimed at the Jewish community. The first is a belief in anti-government conspiracy theories related to a Jewish-controlled "one world government." The second is a prevalence of rightwing extremist chatter on the Internet that focuses on the perceived loss of U.S. jobs in the manufacturing and construction sectors, and home foreclosures they attribute to a deliberate conspiracy conducted by a cabal of Jewish "financial elites.
(Source: Rightwing Extremism: Current Economic and Political Climate Fueling Resurgence in Radicalization and Recruitment, Office of Intelligence Assessment and Analysis, Department of Homeland Security, April 7, 2009.)

- **April 4, 2009:** The New York Police Department beefed up security at the city's synagogues and other Jewish sites amid escalating tensions between Israel and Iran. Concerns that Muslim extremist groups might retaliate against civilians in the city's Jewish community if Israel were to attack Iran's nuclear facilities prompted the NYPD to put together a response plan that includes deploying extra officers, including heavily armed "Hercules Teams," to synagogues, Jewish community centers and Israeli diplomatic offices.
  (Source: Jerusalem Post, 04/04/09)

- **March 24, 2009:** A British terrorist cell with alleged links to Al-Qaeda discussed bombing revelers at a large central London nightclub as well as targeting several synagogues in London and one in Manchester, according to prosecutors. One of the defendants, Salahuddin Amin, even discussed trying to buy a radio-isotope "dirty bomb" from the Russian mafia.
  (Fox News, 03/31/09; European Jewish Press, 03/24/09)

- **February 23, 2009:** FBI Director Robert S. Mueller III warned that extremists "with large agendas and little money can use rudimentary weapons" to sow terror, raising the specter that recent attacks in Mumbai that killed 170 people (including victims at the Chabad House Jewish community center) could embolden terrorists seeking to attack U.S. cities. Mueller said that the bureau is expanding its focus beyond al-Qaeda and into splinter groups, radicals (who come in through the visa waiver program) and "home-grown terrorists." He warned that "melting-pot" communities in Seattle, San Diego, Miami or New York were of particular concern.
  (Source: Washington Post, 02/23/09)

- **February 2, 2009:** According to Michael J. Heimbach, assistant director of the FBI's Counterterrorism Division, Al-Qaida and like-minded individuals are still the country's No. 1 concern in 2009, and that there is significant intelligence out there that indicates their focus remains on the U.S. Threats from Hamas and Hezbollah are quite concerning to the U.S. as well, he stated. In addition, he acknowledged that homegrown extremism is still a significant focus of the FBI, and that we can't lose sight of the domestic terrorism issues, such as White supremacists and neo-Nazi group, who need to remain on the FBI's radar.
  (Source: WTOP (New York), 02/02/09)

- **January 9, 2009:** Terrorist analysts report that throughout the world, Jewish communities will be specifically at risk from several "fatwas" disseminated through Arab media and jihadist websites, including one instructing that "any Jew is a legitimate target that can be struck by Muslims."
  (Source: European Strategic Intelligence and Security Center, 01/09/09)

- **January 6, 2009:** al Qaeda's second-in-command, Ayman al-Zawahiri, called on Muslims to strike at Jewish targets in the West and around the world.
  (Source: Reuters, 01/06/09)

- **January 5, 2009:** Hamas leader, Mahmoud Zahar, called on Palestinian sympathizers to target Jews abroad (including their children) in response to Israel's incursion into Gaza.
  (Source: Associated Press, 01/05/09)

- **May 21, 2009:** The Federal Bureau of Investigation and other cooperating law enforcement agencies arrested four Muslim men as they attempted to carry out a plot to bomb a synagogue and Jewish community center in Riverdale, New York. Law enforcement sources are calling it a homegrown terrorist plot.
(Source: NBC News; Los Angeles Times, 05/21/09)

- **January 1, 2009:** For the third time in a year, a Jewish pre-school was defaced by swastikas and hate speech. Investigators are exploring whether they might be related to Israeli's conflict with Hamas militants in Gaza.
(Source: Ventura County Star, 01/01/09)

- **January 1, 2009:** Jewish day schools in Chicago received a bomb threat in the mail. The letter was sent to the Chicago offices of the Associated Talmud Torahs and the Ida Crown Jewish Academy.
(Source: WBBM newsradio 780; JTA World Report, 01/01/09)

- **September 15, 2008:** Top counterterrorism officials at the U.S. Department of State reiterated a growing refrain among American intelligence agencies that Hezbollah is emerging as an increased threat to the United States (Associated Press, September 15, 2008). The story followed reports in August 2008 that deepening ties between Iran and Venezuela may lead to the establishment of a new Hezbollah front in the western hemisphere to carry out abductions and attacks against Jewish targets (Source: Los Angeles Times, August 27, 2008). Similar reports in June 2008 pointed to warnings raised by intelligence agencies in the United States and Canada that Hezbollah sleeper cells are operating along the U.S. border with Canada, and are poised to mount terror attacks against Jewish targets in the West
(Source: ABC News, June 19, 2008).

- **April 9, 2008:** The U.S. House of Representatives Select Committee on Intelligence held a hearing on "Assessing the Fight Against al Qaeda." On the subject of tactics and targeting al Qaeda will use in the future, counterterrorism experts testified that since 9/11 al Qaeda and its affiliated groups have directed an "intensified campaign" against Jewish targets. Moreover, since 2004, Osama bin Laden has moved the Israeli-American alliance to the center of his justification for al Qaeda's attacks against the west.
(Source: U.S. House of Representatives Select Committee on Intelligence, 04.09/08; Link: http://intelligence.house.gov/Media/Word/Bergen040908.doc)

- **March 4, 2008:** Al Qaeda's second in command, Ayman al-Zawahiri, released an audio tape on March 24, 2008, which called upon al Qaeda followers and sympathizers to attack Jewish interests worldwide. The tape, part of a string of provocative statements by bin Laden and his senior cohorts, was regarded by counter terrorism experts as a new and bold escalation by al Qaeda to link the Middle East conflict with immediate and urgent violence in the West, including against Jewish targets in the United States.
(Source: Associated Press, 03/04/08)

- **February 16, 2008:** With known Hezbollah fundraisers and supporters in the United States, U.S. counterterrorism authorities have been particularly concerned about the threat of Hezbollah sleeper cells against synagogues and other potential Jewish

targets in the United States. On February 14, 2008 the FBI put 101 nationwide Joint Terrorism Task Forces on alert for potential threats against the Jewish community by Hezbollah operatives. (AP, February 14, 2008) A day later, the FBI and the Department of Homeland Security sent out a rare joint bulletin to state and local law enforcement authorities advising them to watch for strikes by Hezbollah against Jewish targets, as well.
(Source: Los Angeles Times, 02/16/08)

- **January 15, 2008:** the Wall Street Journal reported a policy shift within the White House (and among its allies) to place greater pressure on the Iranian regime through an investigation that centers on the **1994 bombing of the AIMA Jewish Community Center in Buenos Aires, Argentina.** In an effort to redefine its Iran policy, the Administration's focus on the JCC bombing, "Serves as a model for how Tehran has used its overseas embassies and relationships with foreign militant groups, in particular Hezbollah, to strike at its enemies.
(Source: Wall Street Journal, 01/15/08)
- **May 1, 2007:** Convicted British homegrown Islamic terrorists with links to the 2005 London subway bombings were in advanced stages of planning, and were **targeting synagogues for attack** when they were arrested.
(Source: CNN.com, 05/01/07)

- **February 13, 2007:** Osama Bin Laden's last known personally authorized terror attacks were made against **two Jewish synagogues in Istanbul.** The simultaneous attacks, in 2003, killed 27 people and injured more than 300.
(Source: Washington Post, 02/13/07)
- The FBI warned Jewish community leaders that Hezbollah operatives were conducting surveillance on **numerous synagogues and Jewish community centers** for possible terrorist attacks in the United States.
(Source: New York Post, 07/19/06)

- **October 10, 2006:** Homegrown Islamic militants were convicted of plotting terrorist attacks against **prominent synagogues and other Jewish iconic sites in Los Angeles.** FBI Director Mueller reported that the group was ready to strike when they were brought down. The plot is considered by counterterrorism officials to be the closest to operationalization since 9-11. Of particular concern, the groups' clandestine terrorist activities were discovered serendipitously during a police investigation into a string of gas station robberies that only later were connected to the funding of the terrorist operation.
(Source: Department of Justice Releases, 7/24/08; 12/14/07; International Herald Tribune 10/10/06)

- **July 28, 2006:** Naveed Haq was found guilty of murder and hate crimes in his second trial for a 2006 **shooting spree at the Jewish Federation of Greater Seattle.** On July 28, 2006, Haq, a Muslim American, attacked the Federation, a center of Jewish communal life and supporter of social welfare, youth and adult education programs. Of the six women he gunned down, one was 17 weeks pregnant and another, Pamela Waechter, died of her wounds. At trial evidence was presented that "he railed against Jews and U.S.-Israeli policies as he opened fire in the Jewish Federation," and that in telephone calls recorded by the King County Jail, Haq told his mother he was "a soldier of Islam."

(Source: Associated Press, 12/15/09; The Seattle Times, 12/15/09; Seattle Post-Intelligencer, 08/06/08; 2008; The Seattle Times, 02/21/08; 07/29/06)

- May 31, 2005: Department of Justice convicted an Iraqi-American who had obtained illegal machine guns and targeted Jewish communal sites in Nashville, Tennessee.
  (Source: Department of Justice Release, 10/08/04; Associated Press, 05/31/05)

- April 13, 2004: Terrorists responsible for the Madrid train bombings in March 2004 also were planning additional attacks on a Jewish community center outside of Madrid, home to the largest Jewish population in Spain, according to evidence gathered in the investigation.
  (Source: New York Times; CNN.com, 04/13/04)

- November 24, 2002: In a "Letter to America" Osama bin Laden released soon after the 9/11 attacks, to explain his reasoning and intent to justify the attacks, he wrote, "The creation and continuation of Israel is one of the greatest crimes, and you are the leaders of its criminals." "This is why the American people cannot be innocent of all the crimes committed by the Americans and Jews against us." The letter also made clear that, to bin Laden, civilian populations, as with governments, were acceptable (equivalent) targets for retaliation.
  (Source: Guardian (UK), 11/24/02; Full text of the letter:
  http://www.guardian.co.uk/world/2002/nov/24/theobserver.)

- June 3, 2002: Abdul Rahman Yasin, one of the terrorists in the first attack on the World Trade Center in 1993, revealed in a CBS 60 Minutes interview that the World Trade Center was not the terrorists' original target. Rather, they initially planned to blow up Jewish neighborhoods in Brooklyn. But after scouting Crown Heights and Williamsburg, they decided to target the World Trade Center, instead. The reasoning: rather than undertaking multiple small explosions in Jewish neighborhoods, they figured that one big explosion in the World Trade Center would kill mostly Jews who they believed made up a majority of the workforce there, according to Yasin's statements.
  (Source: CBS News 06/02/02; Reuters, 06/03/02)

- January 2, 2002: Al Qaeda's training manual, translated by the Associated Press, directed followers to attack Jewish organizations and institutions in every country Jews exist and to carry out the attacks in a manner designed to cause mass causalities.
  (Source: Associated Press, 02/02/02)

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rob.goldberg@jewishfederations.org.

ACCIDENT FUND HOLDINGS, INC.

P O Box 40790
Lansing, MI 48901-7990
www afhi com

September 25, 2013

The Honorable Tim Johnson
Chairman
U.S. Senate Committee on Banking,
Housing and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Mike Crapo
Ranking Member
U.S. Senate Committee on Banking,
Housing and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Johnson and Ranking Member Crapo:

Accident Fund Holdings, Inc. (AFHI) appreciates the opportunity to share our views on the Terrorism Risk Insurance Act (TRIA) program. The combined efforts of our Enterprise make AFHI the 17th largest provider of workers' compensation, and the largest non-governmental specialty writer, in the country. AFHI is a wholly owned subsidiary of Blue Cross Blue Shield of Michigan (BCBSM).

AFHI now employs nearly 1,000 employees throughout the country, writing monoline workers' compensation in all 46 states we're licensed in. In this capacity, and as the former state fund of Michigan, we offer a unique perspective on the TRIA program.

To insure against the peril of terrorism, public/private partnerships such as the TRIA program are necessary. The extension of the federal backstop under the TRIA program continues to have AFHI's full support. TRIA needs to be a long-term solution for workers' compensation insurers and the property casualty industry to protect employers, injured workers and their families. Basic key fundamental reasons for our reauthorization support are:

- Terrorism coverage for workers' compensation insurers cannot be excluded or limited by the policy language. Reinsurers are not able to replace the market capacity created by the expiration of TRIA.

- Workers' compensation insurance is a "no-fault" system, created to provide benefits on behalf of employers to injured workers. Without the extension of the federal backstop, the system designed to protect injured workers will be in jeopardy.

- We are unable to measure the frequency of attacks as we have few data points to model the risk of terrorism in the United States. We do not have a large number of observations to develop credible ratemaking or predictive models for catastrophic risks as a result of terrorism.

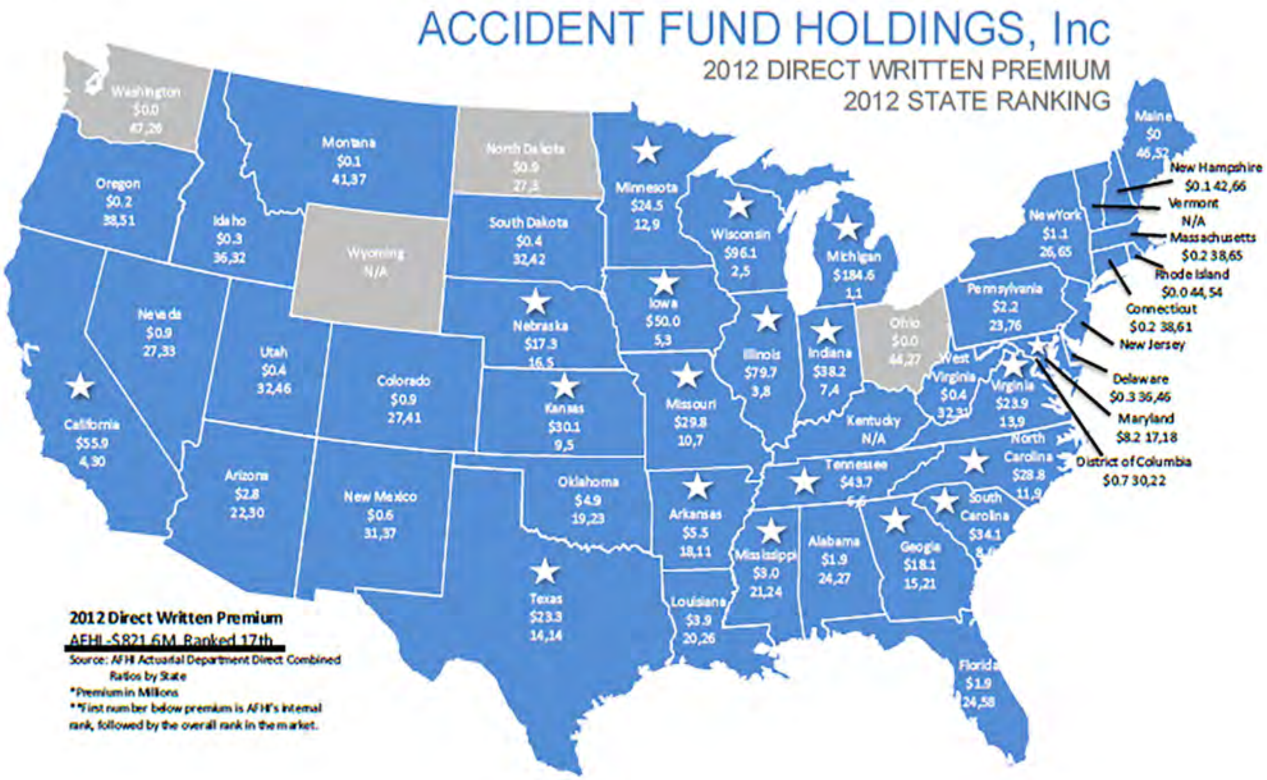
Workers' compensation insurers will need TRIA as long as we need the government to protect us from terrorists. The expiration of TRIA could result in financial insolvency for workers' compensation insurers and the businesses we serve should a nuclear, biological, chemical, radiological attack or a similar catastrophic terrorist event, occur. We would expect to see a migration of business currently being written by private workers' compensation carriers to public state funds, residual markets and guaranty funds for large segments of metropolitan areas. These public options for workers' compensation are not designed to handle a catastrophic terrorist event and they will fail. Injured workers and their families would face potential disruption in benefits.

If the workers' compensation system fails, taxpayers could still be responsible for compensating victims, the very scenario that some policymakers want to avoid by letting TRIA expire. There would be delays in payment and hardship for those injured because of the lack of an efficient compensation system. These disruptions can be averted. Workers' compensation carriers are unable to exclude terrorism or acts of war through policy language like other property casualty writers. Extending TRIA is more than a federal backstop for insurers -- it is a social and economic imperative.

Sincerely,

Steven E. Reynolds
Accident Fund Holdings, Inc.
Vice President, Corporate Secretary & Services

State	2012 DWP	AFHI Rank	Market Rank
Alabama	$1.9	24	27
Alaska	$0.0	48	57
Arkansas	$5.5	18	11
Arizona	$2.8	22	30
California	$55.9	4	30
Colorado	$0.9	27	41
Connecticut	$0.2	38	61
Delaware	$0.3	36	46
District of Columbia	$0.7	30	22
Florida	$1.9	24	58
Georgia	$18.1	15	21
Hawaii	$0.0	43	45
Idaho	$0.3	36	32
Illinois	$79.7	3	8
Indiana	$38.2	7	4
Iowa	$50.0	5	3
Kansas	$30.1	9	5
Kentucky	N/A	N/A	N/A
Louisiana	$3.9	20	26
Maine	$0.0	46	52
Maryland	$8.2	17	18
Massachusetts	$0.2	38	65
Michigan	$184.6	1	1
Minnesota	$24.5	12	9
Mississippi	$3.0	21	24
Missouri	$29.8	10	7
Montana	$0.1	41	37
Nebraska	$17.3	16	5
Nevada	$0.9	27	33
New Hampshire	$0.1	42	66
New Jersey	$0.4	32	77
New Mexico	$0.6	31	37
New York	$1.1	26	65
North Carolina	$28.8	11	9
North Dakota	$0.9	27	3
Ohio	$0.0	44	27
Oklahoma	$4.9	19	23
Oregon	$0.2	38	51
Pennsylvania	$2.2	23	76
Rhode Island	$0.0	44	54
South Carolina	$34.1	8	6
South Dakota	$0.4	32	42
Tennessee	$43.7	6	6
Texas	$23.3	14	14
Utah	$0.4	32	46
Vermont	$0.0	N/A	N/A
Virginia	$23.9	13	9
Washington	$0.0	47	26
West Virginia	$0.4	32	31
Wisconsin	$96.1	2	5
Wyoming	N/A	N/A	N/A


ACCIDENT FUND HOLDINGS, Inc
2012 DIRECT WRITTEN PREMIUM
2012 STATE RANKING
Washington $0.0 47,26
Oregon $0.2 38,51
California $55.9 4,30
Idaho $0.3 36,32
Nevada $0.9 27,33
Montana $0.1 41,37
Wyoming N/A
Utah $0.4 32,46
Arizona $2.8 22,30
Colorado $0.9 27,41
New Mexico $0.6 31,37
North Dakota $0.9 27,3
South Dakota $0.4 32,42
Nebraska $17.3 16,5
Kansas $30.1 9,5
Oklahoma $4.9 19,23
Texas $23.3 14,14
Minnesota $24.5 12,9
Iowa $50.0 5,3
Missouri $29.8 10,7
Arkansas $5.5 18,11
Louisiana $3.9 20,26
Wisconsin $96.1 2,5
Illinois $79.7 3,8
Mississippi $3.0 21,24
Michigan $184.6 1,1
Indiana $38.2 7,4
Kentucky N/A
Tennessee $43.7
Alabama $1.9 24,27
Ohio $0.0 44,27
West Virginia $0.4 32,31
Virginia $23.9 13,9
North Carolina $28.8 11,9
South Carolina $34.1
Geogia $18.1 15,21
Florida $1.9 24,58
Pennsylvania $2.2 23,76
New York $1.1 26,65
Maine $0 46,52
New Hampshire $0.1 42,66
Vermont N/A
Massachusetts $0.2 38,65
Rhode Island $0.0 44,54
Connecticut $0.2 38,61
New Jersey
Delaware $0.3 36,46
Maryland $8.2 17,18
District of Columbia $0.7 30,22
2012 Direct Written Premium
AFHI-$821.6M Ranked 17th
Source: AFHI Actuarial Department Direct Combined Ratios by State
*Premium in Millions
**First number below premium is AFHI's internal rank, followed by the overall rank in the market.

American Bankers Association
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President's Working Group on Financial Markets: Terrorism Risk Insurance Analysis
C/O Kevin Meehan
Federal Insurance Office
U.S. Department of the Treasury
Room 1319
MT, Department of the Treasury
1500 Pennsylvania Avenue NW.
Washington, DC 20220

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

Dear Mr. Meehan:

The American Bankers Association and its insurance and securities subsidiaries, the American Bankers Insurance Association (ABIA) and the ABA Securities Association (ABASA)[1], appreciate the opportunity to provide comments about the long-term availability and affordability of terrorism risk insurance.[2] We believe we are in a unique position to comment since a Financial Holding Company, of which ABA represents many, may act as a lender, insurance broker, and securities underwriter for a variety of large corporate customers. Because of our cumulative experience in these markets, we believe that TRIA is vital to the smooth operation of the capital markets and, therefore, the economy at large.

At the time Congress last considered and passed re-authorization of TRIA in 2007, we commented that TRIA "provides capacity and reliable pricing for terrorism risk insurance in a market that otherwise has been unable to accurately and efficiently price risks associated with terrorist events."

There have been no material changes to the insurance marketplace since then that would compel us to change our opinion. TRIA is necessary to help companies that need terrorism coverage solve the problem of being unable to obtain it.

[1] The American Bankers Insurance Association (ABIA) and the ABA Securities Association (ABASA) are separately chartered trade associations and subsidiaries of the American Bankers Association.
[2] See 78 Fed. Reg. 42588 (July 16, 2013).

Were TRIA to lapse, a variety of undesirable market conditions would result; lenders would not be able to underwrite or syndicate large commercial loans; companies would not be able to secure coverage for terrorism risk, a necessary precedent to securing real estate-related credit; and, existing loans made with the condition that terrorism risk coverage be continuous would be found in default.

Holders and issuers of Commercial Mortgage Backed Securities (CMBS) would also be negatively affected as rating agencies might judge these assets adversely. One rating agency, Fitch, said this:

"Fitch may decline to rate or cap its ratings on CMBS transactions with inadequate terrorism insurance."[3]

While lapse would be the worst possible condition, we also want to point out that market disruptions are being experienced currently due to contract terms extending beyond the expiration date of the program. For example, insurance policies with terrorism coverage for any term extending beyond 2014 can't be issued to commercial customers. Accordingly, multi-year commercial loan products, which require property insurance policies backing them, are at risk now; new loans and refinancing can only be issued on a short term basis or not at all.

We appreciated previous opportunities to provide information to the Treasury. Please find our comments addressing questions regarding coverage and expiration of the TRIA program below.

Coverage

Our members' experiences with terrorism risk insurance have indicated that absent TRIA, the availability of coverage would be minimal and the private insurance marketplace would function inefficiently at best. Previous reauthorizations of TRIA have expanded available coverage and allowed for the market to function in a more effective fashion.

The 2007 reauthorization covered domestic terror events in addition to those of a foreign nature, removing ambiguities about whether a particular event would be covered, or not. Given the events in Boston earlier this year, we find this provision highly relevant. We recommend that this provision remain. It has benefited both policyholders and insurers.

We also want to point out that the most valuable provision in the Act is the "make available" provision, where property and casualty insurers who offer property coverage to a commercial customer must make terrorism coverage available as well. It's critical this provision survive re-authorization too.

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[3] "Fitch Ratings' Report: U.S. Terrorism Reinsurance: Looming Uncertainty of Program Renewal" July 31, 2013

Despite the increased clarity and efficiency afforded by TRIA, corporate insurance customers in high-risk urban areas still encounter difficulty obtaining coverage with sufficient limits. This is due in large part to the inability of the marketplace to ascertain the potential risks of a terrorist event in urban centers and, with confidence, provide the capacity needed to address those needs.

Without TRIA, it is our judgment that coverages for such high risks would be virtually unavailable.

Expiration

We believe it is important to address TRIA re-authorization now, before the program expires at the end of next year. We do not believe states would be able to mandate sufficient policy requirements to protect commercial consumers needing terrorism risk insurance coverage in the absence of this federal program.

In addition, the private sector has not demonstrated an ability to provide terrorism risk coverage at affordable prices, absent TRIA. Terrorism risk cannot be underwritten by traditional means since data on predicted frequency and severity in any given location is unobtainable. As a result, there is no reason to presume that coverage levels and prices would remain consistent if TRIA were allowed to expire.

Conversely, many observers suggest that TRIA inhibits the development of capacity in the traditional re-insurance marketplace. We believe this to be true in principle. Accordingly, to encourage private market development we urge the government to consider reducing the potential liability TRIA represents to the Treasury. Over time, more efficient markets may evolve to a point where TRIA may be discontinued.

We want to point out, however, that several large brokers like Marsh and Willis report that right now, affordable terrorism risk insurance only exists because TRIA does too. We believe them.

Legislative Vehicles

Several bills have been introduced in the House that propose to extend the TRIA program for at least 5 years. This seems to be the minimum practicable extension sufficient to allow insurance markets to respond. Other bills extend the program for 10 years. We are in favor of either approach.

Various enhancements to TRIA are also proposed;

- Changing the aggregate financial responsibility of the Treasury in the event of an attack;
- In addition to the Secretary of the Treasury, including the Secretary of the Department of Homeland Security in the certification process for acts of terrorism; and,
- Changing the "recoupment" provisions TRIA requires the Secretary of the Treasury to impose.

Each of these provisions would enhance the value of the program and we encourage the Administration to support them; however, the most important feature of the legislation is that it suggests the TRIA program be reauthorized promptly.

We strongly support that intent.

Should you have any questions regarding these comments or wish to obtain any further information from the ABA, please contact me at (202) 663-5172 or by email at kmkechn@aba.com.

Regards,

JKAMcKechnie

J. Kevin A. McKechnie
SVP & Director, Office of Insurance Advocacy