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The Center On Federal Financial Institutions (COFFI) is a nonprofit, nonpartisan, non-ideological policy institute focused on federal insurance and lending activities.

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TRIA: Where Do We Go from Here?

The federal government directly participates in the insurance against terrorist attacks of up to $100 billion per year. It does this under the Terrorism Risk Insurance Act of 2002 ("TRIA"), which was enacted in November 2002, and is in effect until December 31, 2005. This law provides a federal financial backstop for the insurance industry for claims from certain terrorist attacks, and requires that every U. S. property and casualty insurance company offer terrorism insurance to its commercial policyholders.

TRIA is currently under review by the U.S. Treasury Department, and new legislation is being proposed in both the House and the Senate to extend TRIA (three bills so far). This paper discusses how TRIA has performed so far and where it may go from here. It is the third in a series of three papers being published concurrently by COFFI. The other two are "Terrorism Risk Insurance Act of 2002: A Primer" and "Terrorism Risk Insurance: Conceptual Issues". The primer explains in non-technical terms how TRIA works and the other paper discusses the issues within a framework of economic and government policy theories surrounding worldwide terrorism today. Please note that COFFI is not advocating any particular policy options in these papers.

I would like to acknowledge the kind assistance of Jeffrey Brown, Doug Elliott, Ellen Seidman and Barbara Stewart. Any mistakes or omissions are, of course, my own.

These papers are dedicated to the memory of Vita M. Marino, who died on September 11, 2001 at Two World Trade Center, New York City.

Please refer to the glossary for an explanation of terms specific to this field.

Executive Summary

To summarize TRIA's stated purposes, it was created to: (1) ensure the widespread availability and affordability of property and casualty insurance for terrorism risk; and (2) allow for a transitional period for the private markets to stabilize, resume pricing for such insurance, and build capacity to absorb any future losses from terrorism risk. There is little dispute, if any, that TRIA has accomplished point (1). The tougher questions arise from the attempt to assess the success or failure of point (2).

In the early days of TRIA, there was concern about the low purchase rate of the coverage mandated under TRIA. Recently, there have been formal surveys conducted that indicate that the purchase rate is increasing, and that prices have fallen slightly. So, while it appears that the private markets are improving with respect to lower prices and an increased number of buyers, this is happening with TRIA as a backstop. As long as TRIA is in effect, it is very difficult to assess how the private markets would react without TRIA. There are, however, many insurance carriers offering stand-alone (non-TRIA) terrorism insurance, and evidence that an increasing number of commercial policyholders are purchasing a combination of the TRIA and non-TRIA coverage.

The Treasury Department is currently conducting its own study of the usefulness of TRIA, and the results of this study are not yet available. No doubt the results of this study will be closely reviewed by policymakers in considering the appropriate future course for TRIA.

During June and July 2004, three Congressional bills were introduced (two in the House, one in the Senate) to extend TRIA for another two years. All three of these bills are designed to extend the current legislation with only minor modifications, essentially adding two more years to the present TRIA structure. This paper compares the details of the three bills that have been proposed.

There are reasonable arguments for and against the renewal of TRIA, as well as various structural options should TRIA be renewed. This paper discusses the pros and cons of renewing TRIA "as is", addresses the merits and disadvantages of including additional types of coverage in the renewed form of TRIA, and discusses some alternative structures that may have some merit for consideration. There is also a summary of terrorism risk programs that have some form of government involvement that are currently in effect in other countries, in order to compare these solutions to the current proposals to extend or modify TRIA.

In conclusion, the "big question" is whether there should be a longer-term federal role in financing terrorism losses. One side of the coin is that the nature of terrorism risk is so closely aligned with governmental actions and restricted information that it is only logical that the government should share in the financial consequences of any future attacks. This implies that it is appropriate for the government to continue to have a role in terrorism risk as long as it is a moderate to severe threat in the U.S., and there should be no effort made to encourage the private markets to take over this risk in its entirety.

The other side of the argument is that there is, or shortly will be, sufficient resources and willingness in the private markets to offer terrorism coverage without TRIA. If this is the case, then it can be speculated that the private markets, while willing, may not ever develop as long as TRIA is in effect, because TRIA provides no incentive for the natural forces of supply and demand in the private markets to take over. By design, TRIA was not intended to be a long-term solution. With that in mind, it seems logical to consider alternative solutions that either involve the government in some different form or allow the private markets to resume on their own once TRIA expires.

One practical question that is oftened ignored in the TRIA debate is whether the existence of TRIA, with its pre-determined co-participation between the public and private sectors, actually restricts the availability of federal funding in the event of a catastrophic terrorist attack. By setting up the TRIA formulas and requirements in advance of any specific terrorism event, the structure of TRIA might serve to limit federal funding that might otherwise have been available.

The question remains as to whether the best solution going forward is some sort of terrorism insurance program that involves federal participation, and if so, what form that should take; or whether TRIA has accomplished its purpose of being a temporary bridge to allow the private markets time to regroup and respond to future terrorism risks.

Table of Contents

Has TRIA fulfilled its purpose?

The stated purpose of the Terrorism Risk Insurance Act of 2002 ("TRIA") is as follows:

To establish a temporary Federal program that provides for a transparent system of shared public and private compensation for insured losses resulting from acts of terrorism, in order to—

1. *protect consumers by addressing market disruptions and ensure the continued widespread availability and affordability of property and casualty insurance for terrorism risk; and*
2. *allow for a transitional period for the private markets to stabilize, resume pricing of such insurance, and build capacity to absorb any future losses, while preserving State insurance regulation and consumer protections.*[1]

There is little dispute, if any, that TRIA has accomplished point (1). TRIA has ensured the widespread availability and affordability of property and casualty insurance for terrorism risk. Treasury has extended the "make available" provisions of TRIA through December 31, 2005, the termination date of the current program. And, based upon the recent studies by Marsh Inc., a major insurance broker, and the Mortgage Bankers Association (MBA), more commercial policyholders have purchased terrorism insurance under TRIA this year than ever before, and rates are at their lowest since the beginning of the program.

The tougher questions arise from the attempt to assess the success of point (2). While it appears that the private markets are improving with respect to lower prices for terrorism insurance and an increased number of buyers, this is happening under the backstop of TRIA. Trade associations for the insurance industry and commercial insurance buyers currently seem to be united in the opinion that TRIA should be extended for another two years, which implies that the private insurance and reinsurance markets are not yet ready to assume terrorism risk on their own by the end of 2005 when the current TRIA expires.

According to an article in the Insurance Journal on June 14, 2004, a broad-based coalition of property-casualty insurance, insurance producer and reinsurance trade associations commended the National Association of Insurance Commissioners (NAIC) for adopting a resolution supporting a two-year extension of TRIA at the NAIC summer meeting in San Francisco.[2] However, the Consumer Federation of America (CFA), which opposed enactment of TRIA and which also opposes it extension, published a report dated April 19, 2004 entitled, "The Terrorism Risk Insurance Act: Should It Be Renewed?"[3] This report is based on a study conducted by CFA taking the view that TRIA is not necessary to ensure the availability and affordability of terrorism insurance for most areas of the country and should be allowed to expire.

While the U.S. has been fortunate not to have had any further terrorist attacks since 9/11, the threat levels remain high, and the possibility of another major attack does not seem to be

[1] TRIA legislation, Sec. 101 (b)
[2] www.insurancejournal.com/news
[3] "The Terrorism Risk Insurance Act: Should It Be Renewed?," by J. Robert Hunter, Director of Insurance, Consumer Federation of America, www.consumerfed.org

diminished. However, in terms of traditional insurance methodology for evaluating risks, it is still too soon to tell whether the events of 9/11 represent a trend or whether they were an isolated occurrence, because the time frame is too short to tell. The fact that the commercial buyers were initially slow to purchase terrorism coverage, and only recently seem to be buying in the volume levels that approach better risk-spreading results for the insurers also represents a short time-frame for evaluation. Therefore, with only another year to go on the current TRIA program, the strong implication from the insurance industry is that more time is required to allow this status to continue and fully develop before any private markets will emerge independent of TRIA. Further discussion on the development of the private markets is included below.

What is being done by Treasury to assess the usefulness of TRIA?

TRIA was enacted as a temporary Federal program that provides for a transparent system of shared public and private compensation for insured losses resulting from acts of terrorism, and mandates a study to be conducted on the effectiveness of the program. According to TRIA, the Secretary [of the Treasury], in consultation with the NAIC, representatives of the insurance industry and of policy holders, other experts in the insurance field, and other experts as needed, shall assess the effectiveness of the Program and the likely capacity of the property and casualty insurance industry to offer insurance for terrorism risk after termination of the Program, and the availability and affordability of such insurance for various policyholders, including railroads, trucking, and public transit. The Secretary shall submit a report to Congress on the results of the study no later than June 30, 2005.[4]

This study, launched in December 2003, is now underway and is expected to provide a better understanding of the types of terrorism coverage offered by insurers and the current level of demand.[5] The results of the Treasury study will undoubtedly influence policymakers as they assess whether TRIA has accomplished its goals and whether it should be extended.

What has been the purchase rate for terrorism risk coverage under TRIA?

TRIA mandates that all U.S. property-casualty insurers must make available terrorism risk insurance coverage, but it does not set the premium rates for such coverage, nor does it set any requirements for businesses to purchase terrorism coverage. The decision to purchase terrorism risk insurance, as made available by insurers under TRIA, is entirely voluntary.

There was some concern shortly after TRIA was enacted that the “take-up rate,” or percentage of commercial policyholders buying terrorism coverage, was low. It is important to note that terrorism coverage, prior to 9/11, was included in commercial insurance policies as part of the package for one price. Historically, the total amounts of any terrorism-related losses had been low, and therefore the coverage was included at no additional charge. Post-9/11, under the “make available” provisions of TRIA, commercial property casualty insurers must offer terrorism risk coverage separately. It is up to the policyholder to accept or decline the coverage. There are

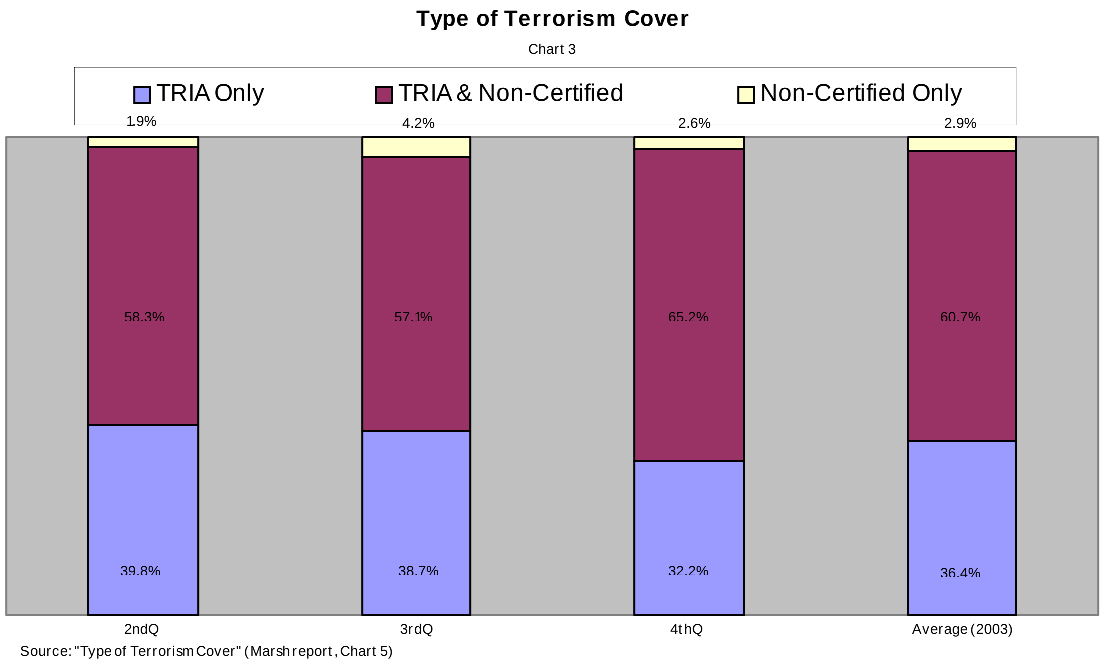
[4] TRIA legislation, Sec. 108 (d)
[5] Kuntreuther, Howard and Michel-Kerjan, Erwann, April 2004, “Dealing with Extreme Events: New Challenges for Terrorism Risk Coverage in the U.S.”, http://grace.wharton.upenn.edu/risk/

no requirements or restrictions on what the insurers may charge for this TRIA-mandated terrorism coverage.

Between April and June 2004, several studies were published on the topic of who is buying terrorism insurance and whether TRIA is achieving its goals of making this insurance available at affordable rates. The results of these various studies provide some interesting data for consideration:

> Marsh, Inc., one of the largest U.S. insurance brokerage firms, announced the results of its terrorism insurance study in May 2004. This study included information on both TRIA and stand-alone terrorism coverage (see explanation of this type of coverage below). Marsh surveyed 2,400 U. S. businesses and found that the median rate for all terrorism insurance dropped by 42% from the second quarter to the fourth quarter of 2003. During the second and third quarters of 2003, the percentages of businesses purchasing the coverage remained relatively flat, at about 25%. In the fourth quarter of 2003, however, the purchase of terrorism insurance was clearly on the upswing. Of all companies with policies renewing in the fourth quarter, the "take-up rate" was approximately one-third, or 32.7%.[6] "As prices have come down, more companies are purchasing terrorism insurance—both under the Terrorism Risk Insurance Act of 2002 and the stand-alone terrorism insurance policies offered by various insurers," said Jill Dalton, a managing director of Marsh and its North American Property Practice Leader.[7]
>
> According to the Marsh study, among all-sized businesses, those with total insured property values between $500 million and $1 billion were most likely to purchase terrorism insurance (both TRIA and stand-alone). Of these firms, 39.7% obtain terrorism insurance, compared to 27.1% of businesses with insured values above $1 billion and 18.2% of those with insured values below $100 million.[8]
>
> From an industry sector perspective, the Marsh study showed the energy sector was the most receptive to the coverage, with more than 40.5% of energy companies purchasing terrorism insurance. At 35.3%, media companies were second, followed by food and beverage companies at 34.7%, habitational and hospitality industries at 31.5%, healthcare at 31.0% and real estate at 30.2%.[9]
>
> The Marsh study breaks down the types of terrorism coverage that companies are buying into the following categories: Non-certified (stand-alone) only; a combination of TRIA and Non-certified; and, TRIA only. As shown in the chart below, there is a gradual trend of fewer companies buying just TRIA and more buying combined TRIA and Non-certified coverage. Overall, the largest category of buyers is the combined coverage group.[10]

[6] Marsh, Inc. research report, "Marketwatch: Property Terrorism Insurance 2004"
[7] Marsh, Inc. press release dated May 10, 2004
[8] Marsh, Inc. research report, "Marketwatch: Property Terrorism Insurance 2004"
[9] Marsh, Inc. research report, "Marketwatch: Property Terrorism Insurance 2004"
[10] Marsh, Inc. research report, "Marketwatch: Property Terrorism Insurance 2004"



Marsh released additional information in June 2004 that showed that 52% of commercial real estate owners purchased terrorism insurance in the first quarter of 2004, up from 28.1% in the fourth quarter of 2003. Overall, 44.2% of U.S. businesses obtained coverage in the first quarter of 2004, also the highest take-up rate since TRIA was signed into law. According to Marsh, some of the increase for real-estate owners in particular also could be attributed to lenders requiring that building owners have the insurance—especially owners in areas perceived to have higher degrees of terror risk. The rise was strongest in central business districts and in the northeast, where there is a higher concentration of tall buildings and financial headquarters. Eric T. Schake, a managing director with Marsh, said the take-up of coverage was greatest among office-building owners, followed by retail-property owners, hotel owners, apartment and condo owners and industrial-building owners.[11]

On June 2, 2004, the Mortgage Bankers Association ("MBA") released the results of a survey it conducted to determine the prevalence of terrorism risk insurance coverage and the impact of the removal of the "make available" provision of TRIA (this study was done prior to the decision announced by the Treasury on June 18, 2004 to extend the "make available" provision through 2005). Of the $656 billion commercial/multifamily debt reviewed in the MBA study, $616 billion, or 93.9%, is required to have terrorism insurance by the mortgage investor and/or servicer. A full $548 billion, or 83.5%, of the outstanding balance of the commercial/multifamily debt reviewed had terrorism insurance in place. According to the survey, insurance specialists at every loan servicer involved in the study expect that if the "make available" provision of TRIA were not extended, terrorism endorsements that are currently in place would be cancelled or excluded. Without the "make available" extension, insurance specialists estimate by the spring of 2005 only 20%, or $132 billion, of their

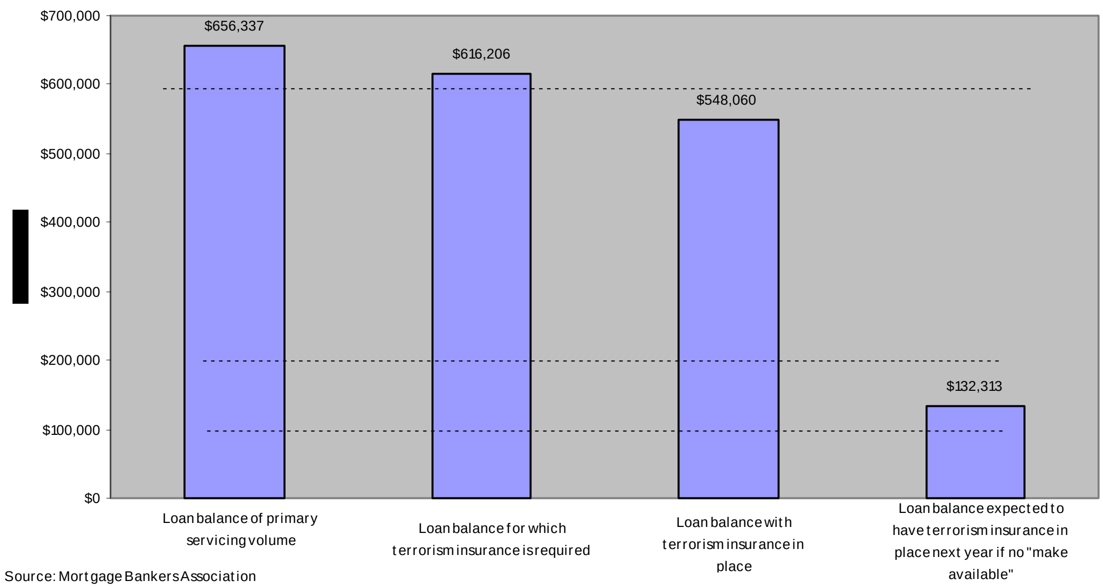
[11] Real Estate Journal, "More Property Owners Seek Terror Insurance," June 21, 2004

> collective portfolios would have terrorism risk insurance coverage in place. This represents a reduction of 75%, or $416 billion, in the balance of loans that would be covered for losses due to terrorism.[12]

The following chart illustrates the survey results regarding loan balances and terrorism coverage[13]:

Loan Balances and Terrorism Coverage

Chart 4



> "The results of this survey clearly demonstrate that terrorism risk insurance is widely used and is more available and affordable today than before TRIA was enacted," said Gail Davis Cardwell, MBA's senior vice president, Commercial/Multifamily group. " In addition, the survey showed that with "make available" in place, 83% of the servicing firms said they expect to always/almost always notify the borrower of requirements and work with him/her to purchase the necessary coverage when adequate coverage is not in place. Twenty-eight percent expect to always/almost always "force-place" coverage, wherein the servicer purchases the coverage and bills the borrower for its cost. However, 44% expect to seldom use this approach."[14]

Prior to these two recent private studies, there was limited information available on the purchase rate of terrorism insurance under TRIA. There was some data suggesting a range between 10 and 30 percent of commercial policyholders had bought terrorism coverage under TRIA. In April 2004, the GAO issued a report entitled, "Terrorism Insurance—Implementation of the Terrorism Risk Insurance Act of 2002". Obviously this report was released prior to having the benefit of the

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[12] Mortgage Bankers Association press release dated June 2, 2004, http://www.mortgagebankers.org/news/index.html
[13] Mortgage Bankers Association TRIA survey results at www.mortgagebankers.org/news. The MBA survey includes information from all of the top 10 commercial/multifamily servicers, as well as 14 of the top 20 and 18 of the top 50 commercial/multifamily servicers, which in total represent one third of the $2 trillion market. The study covered more than 122,800 commercial/multifamily loans. The average loan size covered by the study is $5.3 million.
[14] Mortgage Bankers Association press release dated June 2, 2004

industry studies cited above. The GAO report included the following observations about the purchase rate for terrorism coverage under TRIA:

> While TRIA has improved the availability of terrorism insurance, particularly for high-risk properties in major metropolitan areas, most commercial policyholders are not buying the coverage. Limited industry data suggests that 10 to 30 percent of commercial policyholders are purchasing terrorism insurance, perhaps because most policyholders perceive themselves at relatively low risk for a terrorism event. Some industry experts are concerned that those most at risk from terrorism are generally the ones buying terrorism insurance.[15]

This concern about those most at risk being the only ones to purchase insurance is known in the insurance industry as "adverse selection". It is a general risk that insurance companies must manage, to ensure that their policies are not priced or structured or marketed in such a way as to only attract the highest category of risk. This situation defeats one of the fundamental concepts of insurance, which is spreading risk among as many as possible. A low take-up rate, combined with high-risk buyers, could cause concerns about inadequate spreading of the risk.

The following comments from Gregory V. Serio, Superintendent of Insurance for the State of New York to The Honorable John Snow, Secretary of the Treasury, addressed this concern about the low "take-up rate" and its relationship to "adverse selection":

> "…Concerns raised regarding the low take-up rate may be misplaced for the following reasons. Commercial insureds located in low-risk areas, such as rural communities, will naturally decline coverage because the risk of a terrorist event is low. While some may call this adverse selection, the phenomenon is not unique to terrorism coverage and exists in all lines of insurance. Another reason for electing not to purchase terrorism coverage is driven by the cost of the coverage. Businesses typically do a cost-benefit analysis in determining whether or not to purchase any product or service and in this respect, the decision to purchase or decline terrorism coverage is no different. In order for a business to purchase this coverage, the cost of the coverage must be commensurate with the risk of a terrorist event. Finally, in states that use the Standard Fire Policy, such as New York, any fire loss ensuing from a terrorist attack, whether certified or not, would be covered under the policy, even in situations where the insured has opted not to purchase the TRIA terrorism coverage. The practical effect of some ensuing terrorism losses being covered under the Standard Fire Policy has lessened the demand for TRIA coverage in such states. For these reasons and as expected, participation in TRIA has been directly proportional to the perceived need for the coverage. TRIA has operated exactly as Congress intended; those who needed the coverage purchased it; those who did not need the coverage declined it."[16]

As the purchase rate for terrorism coverage increases, as indicated in the Marsh and MBA studies above, the overall concerns about adverse selection should abate. The broader the policyholder base, the greater the degree of risk-spreading, which serves to diminish the likelihood of any concentration of risk.

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[15] GAO-04-307, a report to the Chairman, Committee on Financial Services, House of Representatives

[16] June 4, 2004 letter from Gregory V. Serio, Superintendent of the State of New York Insurance Department to The Honorable John Snow, Secretary of the Treasury

What is the current status of private markets for stand-alone (non-TRIA) terrorism risk?

Stand-alone, or non-certified, terrorism coverage offers broader protection than TRIA, such as covering domestic terrorism and not being subject to TRIA's certification process for acts of foreign terrorism. Stand-alone policies may also offer coverage for acts of terrorism that occur outside the U.S., for those U.S. businesses that have operatiions overseas. In short, stand-alone policies have more flexibility than the TRIA-only policies, and can be customized to meet the needs of the buyers. For example, if a buisness has overseas terrorism exposure, it could either purchase a stand-alone policy that covers both certified acts in the U.S. (TRIA coverage) and non-certified acts abroad, or it could purchase two separate policies, one for TRIA coverage and one for non-certified coverage abroad. The decision would primarily depend upon the insurer's rates and limits for each type of policy, which in turn depends on the specific details of the exposure. The following chart compares stand-alone coverage with TRIA:

Stand-Alone Terrorism Insurance	TRIA as Part of All-Risk Property
Acts of foreign and domestic terrorism can be covered	Covers foreign acts only
Locations in the U.S. and ex-U.S. can be covered	U.S. locations only
Limits are aggregated or with one or two reinstatement(s)	Per occurrence limits that match property policy limits
Account and terrorism specific deductibles	Deductibles match property policy
Location and schedule specific	Coverage for all locations, including unscheduled, depending on terms of property policy
Non-cancelable policy available	Cancelable terms follow property policy
Long-term policies (up to 3 years) available	Typically one year
Select markets	All markets that meet insurer definition under the Act

Source: Marsh Report, "Marketwatch: Property Terrorism Insurance 2004" [17]

A few insurers began to write limited amounts of stand-alone terrorism coverage during early 2002. However, the amounts of coverage offered were small in comparison to pre-9/11 limits, which were generally equal to policy limits (since terrorism was not previously recognized as a

[17] Marsh Inc. research report, "Marketwatch: Property Terrorism Insurance 2004", printed April 2004 (New York)

distinct risk and was therefore not excluded or otherwise limited). By mid-2002, additional stand-alone capacity had entered the market.[18]

According to The Betterley Report issued in April 2003, there are ten insurers active in the U.S. terrorism marketplace, including ACE, AIG and Lloyd's of London (the three most prominent players) as well as AXIS Specialty, Allied World Assurance (AWACS), Berkshire Hathaway, Endurance Re, Everest Re, Montpelier Re and Renaissance Re. ACE, AIG and Lloyd's are the most active and information about their products is generally available. The others provide coverage which is more customized, therefore not as easily analyzed in a publication format. Betterley concludes that "there is more capacity for terrorism property insurance coverage than many people think, perhaps not as much as had originally been hoped, and certainly not as much as is needed."[19] Of the ten carriers covered in his report, the following limits per location are reported to be available:

ACE USA—$65 million

AIG—$100 million

AWAC—$5 million

AXIS Specialty—$100 million

Berkshire Hathaway—$500 million (possibly as high as $1 billion)

Endurance Re—$5 million

Everest Re—$10 million

Lloyd's of London—$200 million

Montpelier Re—$10 million

Renaissance Re—$50 million[20]

As can be expected, there is little in the way of model pricing for these policies. Premiums are based on exposure, meaning property values, location and security, and have come down since 2002. Betterley concludes that "the interest of insurance companies currently offering terrorism coverage will continue, and that this interest will preserve—and perhaps grow—the market to a healthier level, with broader coverage and lower rates. Unfortunately, increasing capacity and lower rates will only result if attacks cease."[21]

The Marsh report, cited earlier, contains the most recent information on the stand-alone market and reinsurance market. While this survey does not include a list of companies currently writing stand-alone coverage (such as those shown above), it does provide summary information on stand-alone limits and pricing. According to Marsh, limits of up to about $1 billion are available,

[18] Hartwig, Robert, 2002, "September 11, 2001: The First Year. One Hundred Minutes of Terror that Changed the Global Insurance Industry Forever," , Insurance Information Institute paper, http://www.iii.org/media/hottopics/insurance/sept11/sept11paper/

[19] The Betterley Report, "The Terrorism Coverage Market and TRIA: Specialized Coverages When TRIA isn't Enough," by Richard S. Betterley, CMC, April 2003

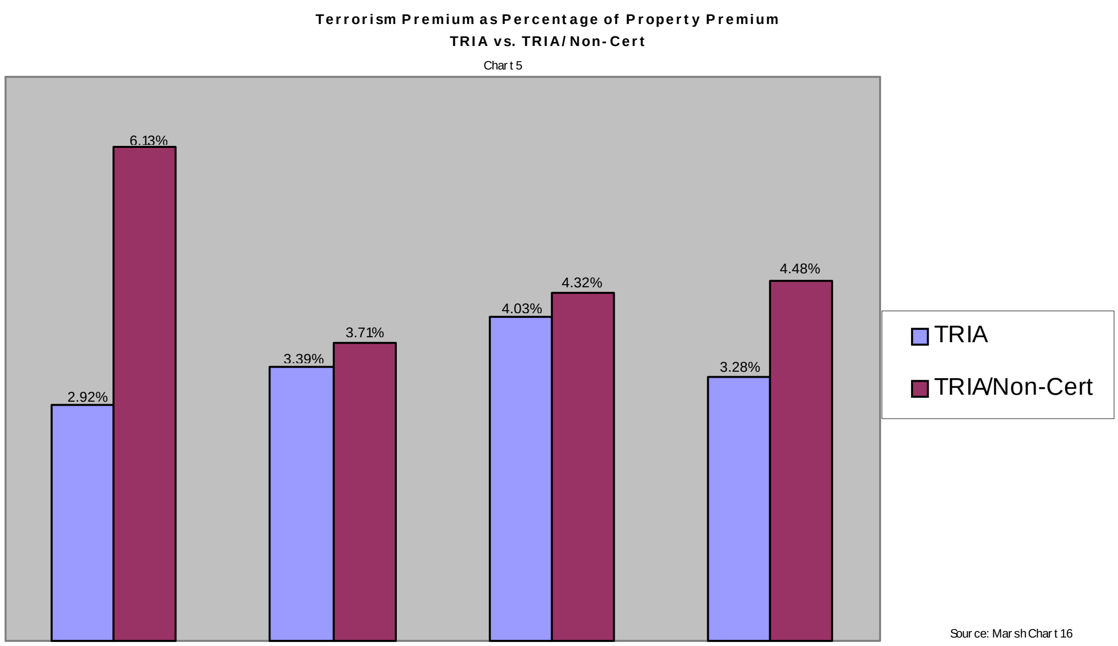
[20] Betterley

[21] Betterley

although limits in the $200 - $500 million range are typically more competitive. Stand-alone programs are sometimes offered in direct competition with TRIA coverage offered by all-risk carriers.

If a location is considered a target risk by property insurers, TRIA pricing from all-risk carriers may be excessive. Stand-alone market pricing is based on "total insured values," or TIV, of the properties being covered, as well as the concentration and location of exposures, and therefore can sometimes be offered at a lower price. For example, the Marsh survey found that for the second and third quarters of 2003, TRIA rates were actually higher than the combined TRIA/non-certified rates. This probably indicates that the companies perceived as having the highest terrorism risk by the insurers were only being offered TRIA coverage, and even then, at a high rate. Risks perceived as lower risks were probably offered the combined coverage, and at a lower price. In the fourth quarter of 2003, the combined rates were higher than TRIA-only rates. As noted earlier, there has been a gradual shift to more buying of the combined cover. This may indicate that insurers are now offering the combined cover to those previously deemed too risky for such a package.[22]

The following chart, from the Marsh survey, illustrates terrorism premiums, both TRIA-only and combined TRIA/non-certified programs, as a percentage of overall property insurance premiums:



According to Guy Carpenter, Marsh Inc.'s reinsurance brokerage affiliate, there is currently a modest amount of reinsurance available for certified terrorist acts. Only a handful of insurers are purchasing this reinsurance to cover their own deductibles, due to its high cost and the relatively low take-up rate for TRIA coverage amoung their policyholders. By contrast, reinsurance for non-

[22] Marsh Inc. research report, "Marketwatch: Property Terrorism Insurance 2004"

certified terrorism is widely available and at reasonable cost. Most insurers are purchasing this in both their risk and catastrophe reinsurance treaties. Whether or not this will continue, and whether or not this will spur the offering of certified reinsurance as retentions increase in 2005, and when TRIA ends, are major questions. If it is offered, pricing and terms will be closely scrutinized.[23]

Should the current form of TRIA be extended?

During June and July 2004, three Congressional bills were introduced, two in the House and one in the Senate, to extend TRIA for another two years. The chart below compares the three bills with the current version of TRIA.

TABLE 6
TERRORISM RISK INSURANCE ACT OF 2002 (TRIA)
COMPARISON OF EXTENTION BILLS

ISSUE	H.R. 4634 (Sessions, et al.)	H.R. 4772 (Capuano, et al.)	S. 2764 (Dodd, Bennett, et al.)
Comparison with TRIA	Identical, except as noted below	Identical, except as noted below	Identical, except as noted below
Length of extension	2 years (until December 31, 2007)	2 years (until December 31, 2008, including a "run-off" in 2008 for policies issued prior to January 1, 2008)	2 years (until December 31, 2007, with a "run-off" until December 31, 2008 for policies issued during 2007)
Lines covered	Identical to TRIA, with a new group life study due by June 1, 2005	Adds group life insurance to the commercial property-casualty lines already covered by TRIA	Directs Treasury to issue rule within 90 days of enactment to include group life insurance on similar terms to commercial property-casualty insurance
Mandatory availability	Extends "make available" requirement through 2007	Extends "make available" requirement through 2007, including any policies that "run off" during 2008	Extends "make available" requirement through 2007, including any policies that "run off" during 2008
Individual insurer deductibles	2006-15% of prior year direct earned premium (DEP) 2007-20% of prior year	2006-15% of prior year DEP 2007-15% of prior year DEP	2006-15% of prior year DEP 2007-15% of prior year DEP

[23] Marsh Inc. research report, "Marketwatch: Property Terrorism Insurance 2004"

	DEP	"Run-Off" Period-15% of DEP for remaining policy term as of the date of insured loss	"Run-Off" Period-Not specified
Trigger for recoupment of "mandatory surcharge" on commercial policyholders	2006-$17.5 billion 2007-$20 billion	Trigger stays at $15 billion through extension period	2006-$17.5 billion 2007-$20 billion
Additional Studies	Treasury Study on long-term alternatives to TRIA due by June 1, 2005	GAO study on TRIA effectiveness and market capacity due by June 30, 2005	Presidential Working Group on Financial Markets study on long-term legislative solutions for terrorism risk insurance due by June 30, 2006 (in consultation with NAIC, industry, and policyholders)

source: www.extendtrianow.org[24]

It is unclear at this point whether any of these bills will make it to a vote during 2004.

From a report prepared by the Property/Casualty Extreme Events Committee of the American Academy of Actuaries, dated May 4, 2004, the following is their list of pros and cons of renewing TRIA "as is" :

TRIA renewed "as is":

Pros:

> *Minimal change and disruption for everyone involved (policyholders, insurers, Congress, Treasury).*
>
> *Current [federal] reinsurance capacity for certified terrorism risk stays in place.*
>
> *Current market stability is retained.*

Cons:

> *Insurer deductible remains at 15 percent of prior year's direct earned premium. It is unclear that this provides sufficient protection from impairment [of] an insurer's ongoing operations or even insolvency.*
>
> *Does not provide for potential improvements to the program.*[25]

While there may be some merit to maintaining the "status quo" simply to avoid further changes in the next three years, it does not seem that the non-TRIA market, nor the terrorism risk

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[24] http://www.extendtrianow.org/news_release.asp?news=127
[25] American Academy of Actuaries, "P/C Terrorism Insurance Coverage: Where Do We Go Post-Terrorism Risk Insurance Act?" prepared by the P/C Extreme Events Committee, May 4, 2004, http://www.actuary.org/pdf/casualty/tria_may04.pdf

reinsurance market is in the same place as it was when TRIA was enacted. There is evidence that the stand-alone terrorism market is improving and that terrorism reinsurance is becoming more widely available. The real question is whether the improvement is enough to handle the demand, or whether, even with the improvement, there continues to be a need for the federal reinsurance program.

In order to thoroughly consider whether TRIA should be renewed as is, a closer look at the status of these two private markets (stand-alone insurance and reinsurance) should be made. If the private market environment today is materially improved, then this information would have a bearing on whether TRIA's purpose has been fulfilled, or whether another three years of the current legislation is in order.

As noted earlier, the major trade organizations for the insurance industry have taken the position that TRIA should be renewed. This position implies that the industry feels that the private markets are not sufficiently developed to sustain the terrorism insurance market without the federal reinsurance provided by TRIA.

The American Academy of Actuaries' paper sets out these discussion points regarding a total expiration of TRIA:

<u>*TRIA expires without alternatives:*</u>

Pros:

> *Reduces federal government involvement in insurance.*
>
> *Forces development of alternative solutions.*

Cons:

> *Although limited coverage is available, insurance industry may be unwilling or unable to provide broad based coverage to all who want it.*
>
> *Might return market to pre-TRIA conditions where availability and affordability were limited.*
>
> *Currently all workers' compensation insurance policies cover terrorism risk (and are required to cover it by state law). Without a federal backstop and without opportunities to manage that exposure through limits and exclusions, availability of workers' compensation insurance will suffer.*
>
> *Increased overall insurance market uncertainty may cause concern in the financial markets*.[26]

The answer to the question of whether TRIA is still needed is highly dependent upon the status of the private markets and especially how these markets would react in the absence of TRIA. Trying to speculate what the markets would look like without TRIA is very difficult to do while TRIA is still in effect.

[26] American Academy of Actuaries, "P/C Terrorism Insurance Coverage: Where Do We Go Post-Terrorism Risk Insurance Act?"

Should additional types of insurance coverage be added to TRIA?

Many questions have been raised over TRIA's treatment of acts of terrorism involving nuclear, biological and chemical (NBC) events. Are losses arising from such events covered or not?

Based upon analysis of TRIA, including opinions from outside counsel, and reviews of various Treasury Department rulings and guidances, it appears that the intent of TRIA is to override only those exclusions created in response to the events of September 11, 2001. However, exclusions that pre-date TRIA, such as those for nuclear exposures or pollution and contamination (which generally apply to losses of a biological or chemical nature), were not intended to fall under the requirement that terrorism insurance must be made available.

While there is no requirement by TRIA that insurers must include NBC events, it appears from the wording of the legislation and further clarification from the Treasury Department that TRIA would cover these types of losses if the underlying policies covered it. For example, workers compensation insurance, which is highly regulated by the state insurance departements, is somewhat unique in that these policies cannot contain any types of exclusions for war, terrorism or NBC exposures. In this case, since the underlying policies cover all these exposures, TRIA would cover them as well.

When Marsh recognized that TRIA would respond to NBC losses if the coverage were available in a policy, it was hoped that insurers would take this opportunity to offer expanded coverage to policyholders and collect additional premiums to fund their TRIA retentions. Unfortunately, due to the nature of the risk, this is almost universally seen as an unpalatable option.[27]

The likelihood of a terrorist attack involving the use of nuclear, biological or chemical agents is difficult to assess, but clearly exists as a possibility. The general lack of coverage for these types of events under TRIA (due to the general use of NBC exclusions prior to 9/11 and after) creates a potential situation where a significant terrorist attack would not be subject to TRIA if it were caused by an NBC event.

Another coverage area currently omitted from TRIA is group life. In compliance with TRIA, Treasury conducted a study of the group life insurance and reinsurance markets, and annouced in August 2003 that they had decided not to include group life, based upon the results of their study. During its evaluation, the Treasury found no appreciable reduction in the availability of group life insurance coverage for consumers, although Treasury did find a current general lack of catastrophic reinsurance for insurance companies that offer group life coverage.[28]

There have been lobbying efforts from the insurance industry to include group life in an extension of TRIA, primarily citing the diminished availability of catastrophe reinsurance as the reason it should be covered by TRIA. All three extension bills address this topic. H.R. 4772 (Capuano et al.) adds group life, and the other two leave it open as a possibility to be determined by the Treasury.

[27] Marsh Inc. research report, "Marketwatch: Property Terrorism Insurance 2004"
[28] Press release from Treasury dated August 15, 2003, http://www.treas.gov/press/releases/js666.htm

What alternative structures, if any, should be considered?

Currently it is unclear what type of terrorism insurance program (if any) will emerge in the U.S. after 2005. One possibility is that TRIA will be renewed with the same or a new risk-sharing arrangement between the insurance industry and the federal government. However, if the program is terminated on December 31, 2005, alternative solutions will undoubtedly be considered. The challenge is to develop a program that will satisfy the different interested parties, each of whom has their own set of values and concerns. In addition to insurance coverage, there are ways of providing protection before an event, so as to reduce the need for the public sector to provide financial aid following a disaster.[29]

It is instructive to consider the private-public partnerships that other countries have established to deal with terrorism risk. Several features of these programs could be considered in developing a sustainable terrorist insurance program in the U.S. after 2005 that involves shared responsibilities between the public and the private sectors.[30]

[29] Kuntreuther and Michel-Kerjan
[30] Kuntreuther and Michel-Kerjan

The following table shows countries with government-backed terrorism insurance plans: [31]

September 11, 2001: One Hundred Minutes of Terror that Changed the Global Insurance Industry Forever

Table 2
Countries with Government-Backed Terrorism Insurance Plans

Country	Provider	Details
U.K.	Pool Re	The international reinsurance market withdrew capacity as a consequence of IRA terrorism in the 1990s, which, in turn, led to a state-supported solution: Limited private cover with additional excess cover for both property damage and business interruption made available for insurance companies to cede to Pool Re (which sets raises and terms). The British government acts as Pool Re's "reinsurer of last resort", in case of insolvency.
Spain	Consorcio	Consorcio CCS (Consorcio de Compensacion de Seguros) is a state insurance facility guaranteeing cover for "extraordinary risks" such as earthquake, volcanic eruption, flood, storm, terrorism and civil commotion. The cover is for property damage only and is integrated into policies issued by private insurance companies which collect premium on behalf of CCS. After deregulation in 1990, it became possible to insure these risks privately, whereupon CCS provided subsidiary cover only and in accordance with the legal minimum. However, policyholders must pay CCS premium in any case and thus maintain the solidarity principle for catastrophic risks.
South Africa	SASRIA	In 1979, South Africa's particular political situation led to the creation of the national institution SASRIA (South African Special Risks Insurance Association) for the (voluntary) insurance of political risks in respect of property damages and, in later, standing charges. While the political situation has improved considerably in recent years, SASRIA still exists.
Israel	PTCF	Terrorism is excluded from standard property policies but the private insurance market grants cover by separate endorsement. Reinsurance coverage is provided by catastrophe excess of loss treaties. In addition, the state of Israel covers property damage losses triggered by politically motivated violence (including terrorism) through the Property Tax and Compensation Fund (PTCF), which was established to cover property losses resulting from war and war-like activities.
Northern Ireland	Government	Terrorism cover for local risk is excluded. Criminal Damage Compensation Order has been in force since 1978 providing compensation on an indemnity basis for property damage and business interruption.
Sri Lanka	Riots and strikes and terrorism fund	Government sponsored riot fund, set up in 1988 includes the risk of terrorism. Limit is Lkr30 million (approximately US$300,000) per risk, per location and is subject to 10 percent deductible.
France	GAREAT	Reinsurance pool established to cover the terrorism exposure of all eligible risks. Membership of the pool is obligatory for all members of FFSA, the French insurers' association. The minimum limit for cover through this scheme is 20% of values or Euro 20 million (US$17.7 million).
Germany	Extremos AG	Specialty terrorism reinsurer set up by the government to offer cover up to €10 billion in excess of €3 billion.

Sources: Swiss Re, Willis

[31] Hartwig

Perhaps the foreign program most often cited as a potentially viable structure that could replace TRIA is the U.K.'s program, Pool Re. This is one of the structures which was discussed during the development of TRIA, and therefore has potential to be reconsidered now as a more permanent alternative to TRIA. The U.K. program established a mutual terrorism reinsurer, Pool Re, funded by the insurers themselves, and with optional participation, but with the government agreeing to cover any losses that exceed the reserve. Arrangements between Pool Re and the U.K. government are designed such that the net cost to the taxpayers is zero over a period of years. As initially proposed in 2002, the U.S. plan would have established a terrorism insurer, the Homeland Security Mutual Reinsurance Company, with federal reinsurance backstop for terrorism losses. Unlike the U.K. plan, the U.S. proposal made the government the "insurer of last resort," i.e., insurers would not have been required to reimburse the federal treasury for reinsurance payments received under the program (Reinsurance Association of America, 2002).

For a number of reasons, the proposal did not gain much traction with the Administration or Congress at the time. Concerns were raised that the mechanism for funding the pool through insurance company contributions was inadequate, and that the government would effectively have to step in at a very low level of any future loss. In addition, many officials were concerned that the insurance pool would turn into a permanent fixture in the insurance industry, leading to a permanent intrusion of the federal government into a traditionally state-regulated industry. Also, concerns were raised about the potential for market power that could develop with only a single, industry-controlled pool. As a result of these and other concerns, it became clear that the insurance industry's reinsurance pool proposal was not going to proceed successfully to legislation back in 2002.[32]

However, three years after 9/11, some things have changed that might make the Pool Re-type of proposal more attractive. The economic environment is stronger than it was in 2001, and without any further terrorism attacks, the crisis mentality has somewhat abated. We have the benefit of having TRIA in effect for two years, which has provided terrorism coverage for commercial policyholders willing to buy it. And, we have the time to consider whether or not it makes sense to have some form of government involvement in a terrorism insurance program, as other industrial countries now have, which is designed to be a longer-term solution than TRIA initially was.

If TRIA continues, will private markets ever develop?

The "big question" of whether private markets will ever develop as long as TRIA is in effect is up for debate. One side of the coin is that the nature of terrorism risk is so closely aligned with governmental actions and restricted information that it is only logical that the government should share in the financial consequences of any future attacks. This implies that it is appropriate for the government to continue to have a role in terrorism risk as long as it is a moderate to severe threat in the U.S., and there should be no effort made to encourage the private markets to take over this risk in its entirety.

[32] Brown, Jeffery, J. David Cummins, Christopher Lewis, Ran Wei, "An Empirical Analysis of the Economic Impact of Federal Terrorism Reinsurance," The Journal of Monetary Economics, Vol. 51, July 2004, pp.861-898

We have been very fortunate to have suffered no certified terrorism events in the U.S. since 9/11. If there is an event that triggers coverage under TRIA between now and the end of 2005, that could become a major factor in the decision of whether or not to extend TRIA, and whether or not the private markets will be ready to assume terrorism risk without the benefit of TRIA or some similar government program. The market for stand-alone terrorism risk is still somewhat fragile. Another certified event, depending on the scale, could cause the market to restrict coverage, increase premiums, or stop writing altogether. On the other hand, such an event could also spur the formation of new capacity by attracting additional capital to expand this private market.

The other side of the argument is that there is, or shortly will be, sufficient resources and willingness in the private markets to offer terrorism coverage without TRIA. If this is the case, then it can be speculated that the private markets, while willing, may not ever develop as long as TRIA is in effect, because TRIA provides no incentive for the natural forces of supply and demand in the private markets to take over. By design, TRIA was not intended to be a long-term solution. With that in mind, it seems logical to consider alternative solutions that either involve the government in some different form or allow the private markets to resume on their own once TRIA expires.

The federal reinsurance provided under TRIA does not replicate private market reinsurance because it is offered without cost, except for the limited mandatory recoupment. The private markets will never be able to compete with that. It can be argued that the insurance industry is reluctant for TRIA to expire, even though it requires each company to offer terrorism coverage (whether they want to or not), because the free reinsurance provided by the government, albeit at catastrophic-event levels, is favored over purchasing reinsurance in the private markets.

However, some insurance companies that currently have very large retentions under TRIA feel that they are providing the coverage without the benefit of much reinsurance anyway. For some of these companies, another loss the size of 9/11 would fall within their retentions. Therefore, they do not see much benefit from TRIA, and in the event that TRIA expires, they would likely continue to offer coverage, although carefully monitoring their accumulations of risk.

Conversely, if an insurer has a relatively small retention under TRIA and expects a sizeable reimbursement from Treasury in the event of a loss, it may be very reluctant to offer coverage without the benefit of federal support (free) versus private reinsurance (market cost).

GLOSSARY

Actuary: A specialist in the mathematics of insurance who calculates rates, reserves, dividends and other statistics.

Adverse Selection: The tendency of those exposed to a higher risk to seek more insurance coverage than those at a lower risk. Insurers generally react either by charging higher premiums or not insuring at all. In the case of natural disasters, such as earthquakes, adverse selection concentrates risk instead of spreading it. Insurance works best when risk is shared among large numbers of policyholders.

Aggregate Limit: Indicates the amount of coverage that the insured has under the contract for a specific period of time, usually the contract period, no matter how many separate accidents might occur.

Assets: Assets for an insurer refer to "all the available properties of every kind or possession of an insurance company that might be used to pay its debts."

Balance Sheet: Provides a snapshot of a company's financial condition at one point in time. It shows assets, including investments and reinsurance, and liabilities, such as loss reserves to pay claims in the future, as of a certain date. It also states a company's equity, known as policyholder surplus. Changes in that surplus are one indicator of an insurer's financial standing.

Business Income Insurance (also known as **Business Interruption Insurance**)**:** Commercial coverage that reimburses a business owner for lost profits and continuing fixed expenses during the time that a business must stay closed while the premises are being restored because of physical damage from a covered peril, such as fire. Business interruption insurance also may cover financial losses that may occur if civil authorities limit access to an area after a disaster and their actions prevent customers from reaching the business premises.

Capacity: The supply of insurance available to meet demand. Capacity depends on the industry's financial ability to accept risk. For an individual insurer, it is the maximum amount of risk it can underwrite based on its financial condition. The adequacy of an insurer's capital relative to its exposure to loss is an important measure of solvency.

A property/casualty insurer must maintain a certain level of capital to underwrite risks. The amount of capital determines how much business it can underwrite, known as its capacity. When the industry is hit by high losses, such as after the 9/11 attacks, capacity is diminished. It can be restored by increases in net income, favorable investment returns, reinsuring more risk and or raising additional capital. When there is excess capacity, usually because of a high return on investments, premium rates tend to decline as insurers compete for market share. As rates decline, underwriting losses are likely to grow, reducing capacity and causing insurers to raise rates and tighten conditions and limits in an effort to increase profitability.

Capital: Shareholder's equity for stock insurers and retained earnings for mutual insurers. The company's capital is measured by the difference between its assets and liabilities. This value protects the interests of the company's policyholders in the event it develops financial problems. From a regulatory point of view, shareholders' interests are secondary to policyholders' interests.

Casualty Insurance: That type of insurance that is primarily concerned with losses caused by injuries to persons and legal liability imposed upon the insured for such injury, or for damage to property of others.

Catastrophe: Term used for statistical recording purposes to refer to a single incident or a series of closely related incidents causing severe insured property losses totaling more than a given amount, currently $25 million.

Catastrophe Model: Using computers, a method to mesh long-term disaster information with current demographic, building and other data to determine the potential cost of natural disasters and other catastrophic losses for a given geographic area.

"Certified" Acts of Terrorism: as defined in TRIA, "certified" acts of terrorism are committed by foreign persons against interests in the U.S. or against certain U.S. interests overseas.

Claim: A demand made by the insured, or the insured's beneficiary, for payment of the benefits of an insurance policy. The dollar amount of a claim is often referred to as a "loss" by insurers.

Commercial Lines: Refers to insurance for businesses, professionals and commercial establishments. Among the major coverages are boiler and machinery, business interruption, commercial auto, comprehensive general liability, directors and officers liability, fire and allied lines, inland marine, medical malpractice liability, product liability, professional liability, surety and fidelity, and workers compensation. Most of these commercial coverages can be purchased separately except business interruption which must be added to a fire insurance (property) policy.

Commissioner of Insurance: The title of the head of most state insurance departments. In some states, the title Director or Superintendent of Insurance is used instead.

Coverage: The scope of protection provided under an insurance policy.

Covered Loss: Illness, injury, death, property loss, legal liability, or any other situation or loss for which an insurer will pay benefits under a policy when such event occurs.

Deductible: The portion of an insured loss to be borne by the insured before he is entitled to recovery from the insurer. Usually it is either a specified dollar amount or a percentage of the claim amount.

Earned Premium: The portion of the premium that applies to the expired part of the policy period (usually one year). Insurance premiums are payable in advance but the insurer does not fully earn them until the policy period expires.

Economic Loss: Total financial loss resulting from (1) the death or disability of a wage earner, or (2) from the destruction of property. Includes the loss of earnings, medical expenses, funeral expenses, the cost of restoring or replacing property, and legal expenses. It does not include noneconomic losses, such as pain caused by an injury.

Effective Date: The date on which the protection of an insurance policy goes into effect.

Exclusion: A provision in an insurance policy that eliminates coverage for certain risks, people, property classes, or locations.

Experience: Record of losses for an insurer, or for the insurance industry as a whole, on either an individual policy, or line of business, or overall.

Exposure: Measure of vulnerability to loss, usually expressed in dollars or units.

File-and-Use Rating Laws: State-based laws which permit insurers to adopt new rates without the prior approval of the insurance department. Usually insurers submit their new rates with supporting documentation.

General Liability Insurance: Insurance designed to protect business owners and operators from a wide variety of liability exposures. Exposures could include liability arising from accidents resulting from the insured's premises or operations, products sold by the insured, operations completed by the insured, and contractual liability.

Incurred Losses: The losses occurring within a fixed period, whether or not adjusted or paid during the same period.

Insurable Risk: Risks for which it is relatively easy to get insurance and that meet certain criteria. These include being definable, accidental in nature, and part of a group of similar risks large enough to make losses predictable. The insurer also must be able to come up with a reasonable price for the insurance.

Insurance: A system to make large financial losses more affordable by pooling the risks of many individuals and businesses and transferring them to an insurance company in return for a premium.

Insurance Department: In the U.S., a governmental bureau in each state charged with the administration of insurance laws, including the licensing of agents and insurers and their regulation and examination. In some jurisdictions the department is a division of another state department or bureau.

Insurance to Value: Insurance written in an amount approximating the value of the property insured.

Insured: The party to an insurance agreement whom the insurer agrees to indemnify for losses, provide benefits and render services to.

Insurer: The party to an insurance agreement who undertakes to indemnify for losses, provide pecuniary benefits and render services.

Limits: Maximum amount of insurance that can be paid for a covered loss.

Line: Type or kind of insurance, such as personal lines or commercial lines.

Loss: Generally refers to (1) the amount of reduction in the value of an insured's property caused by an insurable event, (2) the amount sought through an insured's claim, or (3) the amount paid on behalf of an insured under an insurance contract.

Loss Frequency: Number of times a loss occurs. One of the criteria used in calculating premium rates.

Loss Reserve: The estimated liability, as it appears in an insurer's financial statement, for unpaid insurance claims or losses that have occurred as of a given evaluation date. For individual claims, the loss reserve is the estimate of what will ultimately be paid out on that claim.

Loss Severity: The dollar amount of a loss. One of the criteria used in calculating premium rates.

"Make Available" Provisions: In TRIA, these require that each insurer must make available, in all of its commercial property and casualty insurance policies, coverage for losses due to covered acts of terrorism that does not differ materially from the terms, amounts and other coverage limitations applicable to losses arising from events other than acts of terrorism.

National Association of Insurance Commissioners (NAIC): An association of state insurance commissioners formed for the purpose of exchanging information and of developing uniformity in the regulatory practices of the states through drafting model legislation and regulations. The NAIC has no official power to enforce compliance with its recommendations.

Occurrence: An event that results in an insured loss.

Personal Lines: Property/casualty insurance products that are designed for and bought by individuals, such as homeowners and automobile policies.

Policy: A written contract for insurance between an insurance company and policyholder stating details of coverage.

Premium: The price of an insurance policy for a given period of time, usually one year.

Property/Casualty Insurance: Covers damage to or loss of policyholder's property, and legal liability for damages caused to other people or their property. Property/casualty insurance is one segment of the insurance industry (the other is life/health). It includes auto, homeowners and commercial insurance. Outside the United States, property/casualty insurance is referred to as nonlife or general insurance.

Rate: The cost of a unit of insurance, usually per $1000 of coverage. Rates are based on historical loss experience for similar risks and may be regulated by state insurance departments.

Reinsurance: Insurance bought by insurers. A reinsurer assumes part of the risk and part of the premium originally taken by the insurer, known as the primary company. Reinsurance effectively increases an insurer's capital and therefore its capacity to sell more coverage. The business is global and some of the largest reinsurers are based abroad. Reinsurers have their own reinsurers, called retrocessionaires. Reinsurers don't pay policyholder claims directly; they reimburse the insurers for claims paid.

Reserves: (See "Loss Reserves").

Risk: The chance of loss for the person or entity that is insured, or the specific event for which the policyholder is insured.

Solvency: Insurance companies' ability to pay the claims of policyholders. Regulations to promote solvency include minimum capital and surplus requirements, statutory accounting conventions, limits to insurer's investment and corporate activities, financial ratio tests, and financial data disclosure.

Standard Policy: (1) Coverage which has identical provisions regardless of the issuing insurer. Many common policies are standardized. (2) Insurance issued to a standard, or "average", underwriting risk.

Stand Alone Terrorism Insurance: Terrorism insurance coverage offered by insurers which is not subject to the terms and conditions under TRIA. Such coverage may offer broader terms, such as coverage for both foreign and domestic acts of terrorism, as well as coverage for locations outside of the U.S. This law provides a federal financial backstop for the insurance industry for claims from certain terrorist attacks, and requires that every U. S. property and casualty insurance company offer terrorism insurance to its commercial policyholders.

Sublimit: Any limit of insurance which exists within another limit. For example, special classes of property may be subject to a specified dollar limit per occurrence, even though the policy has a higher overall limit.

Surety Bond: A contract guaranteeing the performance of a specific obligation. It is a three-party agreement under which one party, the surety company, answers to a second party, the owner, creditor, or "oblige", for a third party's debts, default or nonperformance. Contractors are often required to purchase surety bonds if they are working on public projects. The surety company becomes responsible for carrying out the work or paying for the loss up to the bond "penalty" if the contractor fails to perform.

Surplus Lines: Property/casualty insurance coverage that isn't available from insurers licensed in the state, called admitted companies, and must be purchased from a non-admitted carrier. Examples include risks of an unusual nature that require greater flexibility in policy terms and conditions than exist in standard forms or where the highest rates allowed by state regulators are considered inadequate by admitted companies. Laws governing surplus lines vary by state.

Terrorism Coverage: Included as part of the package in standard commercial insurance policies before September 11, 2001, virtually free of charge. Since September 11, terrorism coverage is priced and sold separately, either under the terms of TRIA, or as Stand Alone coverage.

Terrorism Risk Insurance Act of 2002 (TRIA): This law provides a federal financial backstop for the insurance industry for claims from certain terrorist attacks, and requires that every U. S. property and casualty insurance company offer terrorism insurance to its commercial policyholders.

Underwriting: The process of selecting risks for insurance and classifying them according to their degrees of insurability so that the appropriate rates may be assigned. The process also includes rejection of those risks that do not qualify.

Underwriting Income: The insurer's profit (or loss) on the insurance sales after all expenses and losses have been paid. When premiums are not sufficient to cover claims and expenses, the result is an underwriting loss. Investment income is not included in this amount.

Workers Compensation: Insurance that pays for medical care and physical rehabilitation of workers injured on the job, and helps to replace lost wages while they are unable to work. State laws, which vary significantly, govern the amount of benefits paid and other compensation provisions.

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