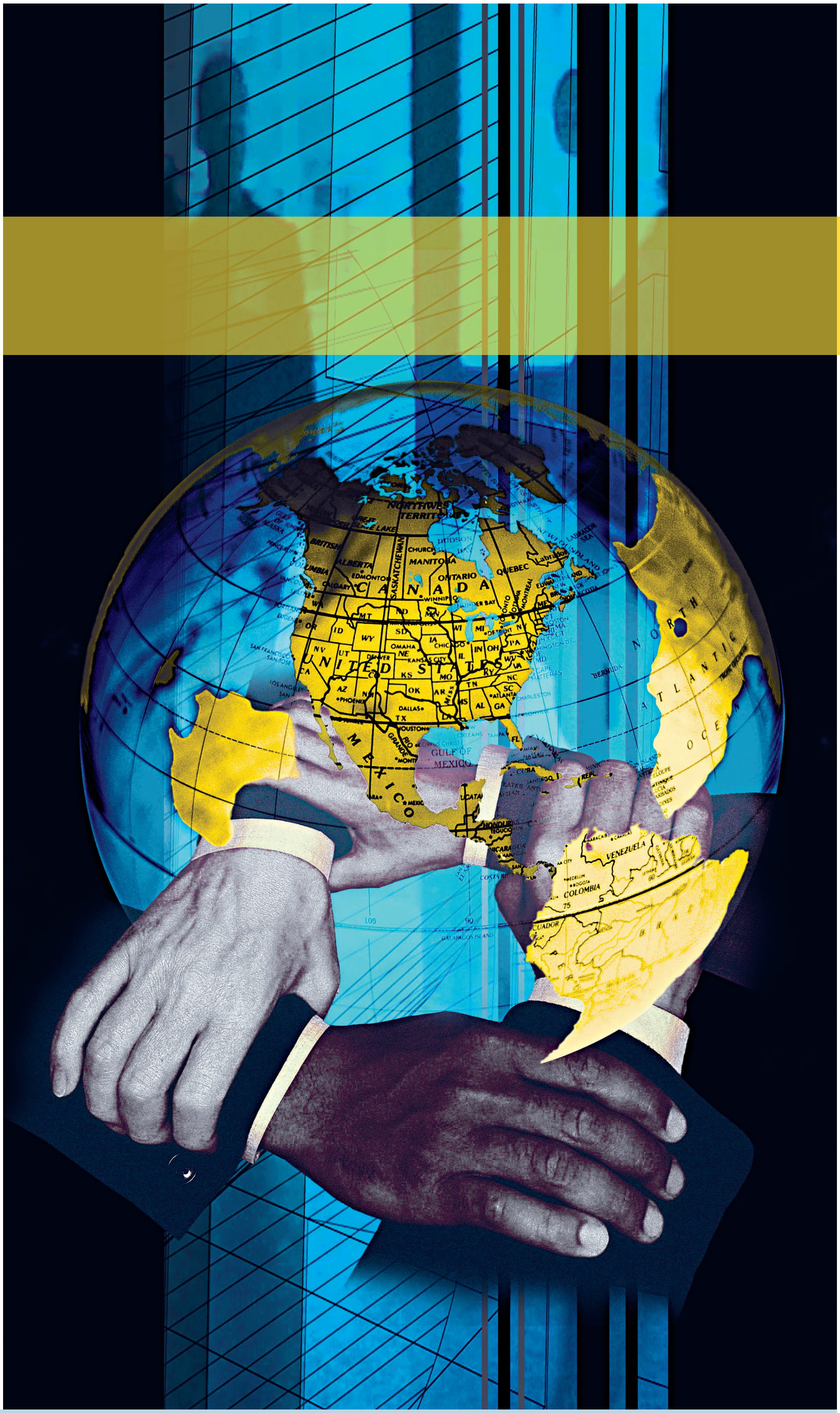
Terrorism Risk Insurance

By Ronald R. Robinson



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At the Crossroads Yet Again

Terrorist acts are brutal, random, and usually visited on a nation's civilian population. Terrorism's goal is to coerce that population to alter the policies and conduct of their government to advance the terrorists' agenda. Terrorism's weapon of choice is the indiscriminate and violent destruction of life and property, which is intended to erode a nation's sense of security and to drive its government's economic and political decisions by fear, not free choice.

Insurance's goal is the protection of life and property and the preservation of security to help assure that economic and political choices are made without fear. Thus, insurance can unswervingly attack the terrorists' agenda by accepting the transfer of a nation's terrorism risk from its civilian population to a solvent and effective coverage mechanism. This is what the United States accomplished when the federal government created the Terrorism Risk Insurance Act of 2002 (TRIA).

The TRIA program became law just 14 months after the September 11, 2001, terrorist attacks. Congress created TRIA in response to terrorism risk exclusions that were added to most property and casualty policies following the $40 billion loss resulting from those attacks. The TRIA program provides $100 billion in terrorism risk insurance through a unique underwriting partnership between private insurance markets (approximately $35 billion) and the federal government (approximately $65 billion) that covers losses from future attacks. This was not a unique political choice for this risk in 2002: Great Britain, France, Germany, Portugal, Spain, and Israel, to name a few countries, already had or soon created similar insurance mechanisms. All of these foreign programs, though evolving, remain in force today. The United States' TRIA Program must be re-authorized this year or it will end. Herewith your field guide to the debate over its future and why re-authorization is the only sound choice.

Do We Need Terrorism Risk Insurance?

The core function of insurance is to support the economic infrastructures and civil justice systems of nations that want to remain, or to become, democracies. A free economic infrastructure exists, in large measure, because first-party property coverage protects it from unmitigated loss. Third-party coverage also protects the financial foundations of the United States in the following ways: (1) professionals are protected in their practices by errors and omissions policies; (2) corporate operations are protected by directors' and officers' policies; and (3) workers are protected by workers' compensation policies. In our private lives, we are protected by the various first- and third-party personal lines of insurance, including auto, home, health, and life coverage.

Insurance also assures business and private citizens that they will always have the protections of the civil justice system. Third-party casualty insurance coverage (1) pays the counsel that protects the defendant, (2) pays civil settlements and awards, and (3) pays the plaintiff's counsel through those settlements and awards. Moreover, the civil justice system provides redress when access to our nation's economic infrastructure is not equally accessible to all and our civil rights are endangered.

Terrorism's threat to our financial foundations and our civil rights are risks that must be transferred if our economic and political choices are to remain free from fear. Yes, we need terrorism risk insurance because it is essential to the preservation of democracy. Next question.

Can Terrorism Losses Be Insured?

One hundred years ago, most of the covered risks that we take for granted today were, if discussed at all, considered uninsurable. However, insurance markets did not wait for sure bets to create new insurance products. Private enterprise and competition for market share drove the innovation that evolved into today's multifaceted risk transfers. Over the last century, underwriters, actuaries, claims professional, policyholders, coverage lawyers, and risk analysts met, studied, made calculated assumptions, and refined their insurance products to expand market offerings and new coverage. Over the last decade, hundreds of terrorism insurance risk transfer professionals have worked to strengthen the underwriting of this coverage, lessen aggregation of its losses, and properly rate its premiums. Obviously, terrorism risk coverage is not a sure bet, but the industry has done what it has always done well—taking the bet now and striving to improve its odds over time. More importantly, it has been starkly evident since September 12, 2001, that the time to muster the country's full economic forces is not after a terrorist attack. Yes, the risk is insurable. Next question.

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Who Should Assume the Transfer of Terrorism's Risks?

The *sine qua non* of insurance has always been "loss prediction and control." To quantify and rate a risk requires predicting loss and exercising control over the factors that create it as much as possible. As part of that process, property and casualty insurance "loss control" experts have historically "walked an insured's plant" to identify, quantify, prevent, or limit hazards. In that process, "loss control" experts have also analyzed an insured's operations, products, services, and manufacturing processes to lower risks and properly rate premiums to assure solvent coverage.

Governments are uniquely suited to "walk the global plant," so to speak, to analyze the weapons, finances, recruitment, command, targets, and operations employed by terrorists to identify, quantify, prevent, or limit their attacks. Neither private market insurers nor their insureds are equipped to address, let alone handle, the "loss control" needed for terrorism risks. Moreover, the federal government has the loss control obligation for this risk because it arises from the economic and political policies of the Congress and Administration. These are the triggers for a terrorist attack. Hand in hand with this obligation is the oldest principle of democracy: government must have a stake in the losses that flow from the risk that it creates and that only it can possibly control.

Some would argue that governments should completely assume this risk. However, governments do not have the private market's expertise, honed through experience in a competitive environment for over one hundred years, to underwrite and rate terrorism risk. Moreover, most governments are not equipped to handle claims or to manage their defense. The insurance industry is more capable for this role. Consequently, still others would argue that insurers should completely assume this risk because of the industry's current $600 billion policy surplus. However, insurers have no access to the only loss control mechanism that could possibly lessen the risk that they would be called upon to cover alone.

The most efficient and successful transfer choice for this unique risk is to create and sustain this coverage by pairing carrier capital, private market investment capacity, and their joint private marketplace experience, with the financial and globally strategic military resources of government. TRIA is a partnership that blends the strengths of government and the expertise of the insurance industry to create a program that provides the security that democracies need to respond effectively to terrorist acts. Now is time to ask how to improve TRIA, not to debate how to dismantle it, or which partner to fire.

TRIA—At the Crossroads Yet Again

TRIA was originally a three-year program, set to be reevaluated in 2005. The renewal debate in 2005 was centered on the same three basic questions posed when TRIA was adopted: (1) do we need a federal terrorism risk insurance program; (2) can terrorism losses be insured; and (3) who should assume the transfer of terrorism's risks, private markets, the government or a partnership of them both? TRIA was renewed for two years through 2007. In 2007, this same debate was reprised, but at the eleventh hour, TRIA was reauthorized for seven years, through December 31, 2014. The debate over the survival of TRIA is about to commence in Congress. Three trial balloons are afloat in the form of two proposed amendments in the House and one in the Senate.

The recent Report of the President's Working Group On Financial Markets on The Long Term Availability and Affordability of Insurance for Terrorism Risk (April 2014; 37 pages; "PWG Report") should clarify and focus the issues in the renewal debate. It explains and demonstrates, with facts and studies, with detail, that: (1) do we need a federal TRIA program to protect our economy; (2) this risk can be insured; and (3) a partnership of the federal government and private markets is a sound, viable and solvent solution. What should be before us, therefore, is not a replay of the old three question debate, but rather a discussion focus on long neglected and significant questions: (1) is it necessary to expand the scope of TRIA beyond workers' compensation, property, and casualty lines to encompass errors and omissions, directors and officers, and personal lines that directly protect main street Americans; (2) does coverage for cyber-attacks require any clarification; and (3) will chemical, biological, and nuclear losses be covered?

What Is DRI Doing in the TRIA Debate?

In 2003, private market insurance professionals from the United States and the United Kingdom created an initiative to assist Congress in reauthorizing TRIA (2002), in 2005. Most participants were DRI members and included in their ranks coverage attorneys, brokers, underwriters, claims managers, actuaries, risk analysts, antiterrorism experts, and senior insurance executives. In 2004 DRI Insurance Law Committee Chair Jeannie Ungar recommended that this group become an Insurance Law Committee Subcommittee. The DRI Insurance Law TRIA Subcommittee was instrumental to achieving and shaping the 2005 two-year extension of the TRIA program and again to its 2007 seven-year extension, through December 31, 2014. The chair of the U.S. House Financial Services Committee commended the subcommittee, acknowledging that it had changed the course and the content of the 2007 TRIA reauthorization act.

The TRIA Subcommittee will again offer its services to Congress and the Administration by working with the U.S. Senate Banking Committee, the U.S. House Financial Services Committee, and the U.S. Treasury Department to extend TRIA beyond 2014. Assistance will take the form of white papers on TRIA issues, comments on proposals made to Congress and the U.S. Treasury by stakeholders in the TRIA reauthorization process, and presentations in forums that debate terrorism risk insurance programs. In 2004, DRI will host a webpage that can be accessed by anyone in Congress and all of the stakeholders in the reauthorization process, which will house all of the Subcommittee's new white papers, relevant prior white papers the PWG Report and other resources.

The Mission of the DRI Insurance Law Committee TRIA Subcommittee

Since 2004, the DRI Insurance Law Committee TRIA Subcommittee has sought to sustain a viable TRIA program. Over the past 10 years the subcommittee has (1) promoted debate at public and private forums on the insurability and risk transfer questions raised by terrorism insurance in general and TRIA in particular, partly by presenting subcommittee white papers at terrorism risk seminars in the United States, China, Italy, Portugal, Spain, and the United Kingdom; (2) provided nonpartisan, objective analysis and commentary on the issues involved in that debate; (3) fostered interest and participation in the debate by insurance professionals and experts, as well as the public at large; (4) supported private market claim handling and resolution of all TRIA claims within the claims' layers of loss, unless a loss implicated the federal layer of coverage, which will render claims handling and resolution to the province of the U.S. Treasury Department, which in turn will consult with the private markets; and (5) called upon Congress, the U.S. Treasury Department, and the administration to ensure the continuation of a solvent, broad-based, and responsible terrorism risk insurance program in the United States, to be founded on a partnership between private insurance markets and the federal government.

The Rules of Engagement for the DRI Insurance Law Committee TRIA Subcommittee

DRI Insurance Law Committee TRIA Subcommittee members do not, on behalf of DRI, advocate for or against any debated TRIA proposal or provision. When testifying, writing, or commenting on TRIA issues, subcommittee members and white paper authors adhere to the mission stated above. When providing their own comments and opinions on the issues involved in the TRIA debate, however, subcommittee members speak as individuals, based on their own expertise. The discipline exercised by members in following these rules has earned the respect of all the stakeholders in the TRIA debate, who value the subcommittee's nonpartisan commentaries and opinions.

DRI Welcomes You to Join the Insurance Law Committee TRIA Subcommittee

We invite you to join the subcommittee. Here is all that you have to do to become a member: (1) provide your services on a pro bono basis and cover your own expenses; (2) do not accept any financial support for services or expenses attendant to your participation; (3) adhere to the mission and the rules of engagement; and (4) check all other agendas at the door to serve your country in its response to terrorism with your independent expert analysis, advice, and presentations. The subcommittee receives logistical support from DRI on a par with any other DRI committee. You can become part of a unique group of people who want to use their expertise to do something of value in the fight against terrorism. We invite you to bring your talents to the table.

The members of DRI Insurance Law Committee TRIA Subcommittee in 2014 who invite you to join them include chair and co-founder of the subcommittee, Ronald R. Robinson, Berkes Crane Robinson & Seal, Los Angeles, CA; vice chair and co-founder of the subcommittee, Kim G. Quarles, Senior Vice President, Willis, New York, NY; subcommittee co-founder, Donald W. Goodrich, former co-chair of the Families of Sept. 11 Group, Donovan & O'Connor, Dover, MA; chair of the DRI Insurance Law Committee, Michael M. Marick, Meckler Bulger Tilson Marick & Pearson, Chicago, IL; DRI Center for Public Policy liaison, Jill Cranston Rice, Dinsmore & Shohl, Morgantown, WV; DRI staff liaisons to the subcommittee, Tyler Howes, Tim Kolly, and Kelly Tiffany; Richard L. Angell, Zupkus & Angell, Denver, CO; John C. Bonnie, Weinberg Wheeler Hudgins Gunn & Dial, Atlanta, GA; Kate Browne, Senior Vice President, Swiss Reinsurance America, New York, NY; Brandt Gerard Cordelli, The Coverage Law Firm, Washington, DC; Joseph M. Goldberg, Sentry Insurance Company, Stevens Point, WI; David Golden, Property Casualty Insurers Association of America, Chicago, IL; Matthew M. Haar, Saul Ewing, Harrisburg, PA; Jay Barry Harris, Fineman Krekstein & Harris, Philadelphia, PA; Gregory J. May, Nelson Mullins, Boston, MA; James A. McFall; Neil Dymott Frank, San Diego, CA; Clive O'Connell, Goldberg Segalla, London, UK; William D. Riley, Paul Frank & Collins, Burlington, VT; L.D. Simmons II, McGuireWoods LLP, Charlotte, NC; Dale O. Thornsjo, O'Meara Leer Wagner, Minneapolis, MN; Jeanne H. Unger, Bassford Remele, Minneapolis, MN; and Gordon Woo, Ph.D., Risk Management Solutions, London, UK.

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