

# Report of the President's Working Group on Financial Markets

## Market Conditions for Terrorism Risk Insurance 2010



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## Executive Summary

The terrorist attacks of September 11, 2001, occurred a little over nine years ago. The Terrorism Risk Insurance Program (“Program”), a temporary government intervention in the private insurance market for terrorism risk insurance coverage, is now entering its eighth year. As mandated by the Terrorism Risk Insurance Act of 2002 (Pub. L. 107-297, 116 Stat. 2322) (“TRIA”), as amended, the President’s Working Group on Financial Markets (“PWG”)<sup>1</sup> has performed an on-going analysis of market conditions for terrorism risk insurance. This is the PWG’s second report of its findings to Congress; its first report was provided in 2006 (“2006 Report”). The key findings of this Report are:

- The availability and affordability of terrorism risk insurance provided by the private sector has improved since 2006. Since the PWG’s last report to Congress, insurers have built capital and increased marketplace capacity.
- Overall, marketplace terrorism risk insurance capacity has increased, and significantly in some forms. Nevertheless, capacity is constrained in some markets (e.g., high-risk geographic locations and properties), and some commercial insurance policyholders in high-risk urban areas have difficulty obtaining coverage with sufficient limits.
- Improvements in the terrorism risk insurance market may have occurred due to improvements in modeling and managing accumulation and concentration of aggregate loss exposure; new market entrants and increased competition; and heightened capital positions of the property and casualty insurance and reinsurance industries. The industry better understands aggregate risk and the increased capacity and competition have resulted in decreases in price generally.
- Take-up rates among commercial insurance policyholders reached approximately 60 percent in 2006, but have remained roughly flat since then. Among those commercial insurance policyholders taking up terrorism risk insurance, there is some indication that more coverage, as measured by policy limits, may be being purchased.
- Market participants (policyholders, insurers, and reinsurers) remain uncertain about the ability of models to predict the frequency and severity of terrorist attacks. Such views influence policyholder perception of risk and purchase decisions, as well as insurer and reinsurer capacity allocations.

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<sup>1</sup> The PWG (established by Executive Order 12631) is comprised of the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, the Chairman of the Securities and Exchange Commission, and the Chairman of the Commodity Futures Trading Commission. Executive Order No. 12,631, 53 Fed. Reg. 9421 (March 18, 1988).

## **Background**

The Program was established on November 26, 2002, immediately upon TRIA being signed into law. The Program is administered by the Department of the Treasury.

The Terrorism Risk Insurance Extension Act of 2005 (Pub. L. 109-144, 119 Stat. 2660), which amended TRIA, provided that the PWG perform an analysis regarding the long-term availability and affordability of insurance for terrorism risk, including group life coverage; and coverage for chemical, nuclear, biological, and radiological (“CNBR”) events. In the third quarter of 2006, the PWG submitted a report of its findings to Congress.<sup>2</sup>

The Terrorism Risk Insurance Program Reauthorization Act of 2007 (Pub. L. 110-160, 121 Stat. 1839) further amended TRIA and mandated that the PWG perform an ongoing analysis of the long-term availability and affordability of insurance for terrorism risk and to report to Congress in 2010 and 2013.

## **Report Mandate**

Section 108(e) of TRIA, as amended, provides:

### **(e) ANALYSIS OF MARKET CONDITIONS FOR TERRORISM RISK INSURANCE.**

(1) IN GENERAL. The President’s Working Group on Financial Markets, in consultation with the National Association of Insurance Commissioners, representatives of the insurance industry, representatives of the securities industry, and representatives of policy holders, shall perform an ongoing analysis regarding the long-term availability and affordability of insurance for terrorism risk.

(2) REPORT. Not later than September 30, 2006, and thereafter in 2010 and 2013, the President’s Working Group on Financial Markets shall submit a report to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives on its findings pursuant to the analysis conducted under subsection (1).

## **Findings of the PWG’s 2006 Report to Congress**

Some of the key findings of the 2006 Report<sup>3</sup> were:

- The availability and affordability of terrorism risk insurance improved from 2001 to 2006, despite the increases in insurer retentions under TRIA. Insurers were allocating additional capacity to terrorism risk, prices were declining, and take-up (purchase) rates were increasing.

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<sup>2</sup> That report, Terrorism Risk Insurance (Sept. 2006) (“2006 Report”) can be found at <http://www.treasury.gov/resource-center/fin-mkts/Documents/report.pdf>.

<sup>3</sup> 2006 Report at 1-6.

- The improvement in the terrorism risk insurance market was due to several important factors including: better risk measurement and management, improved modeling, greater reinsurance capacity, and the recovery in the financial condition of property and casualty insurers.
- Take-up rates increased as prices fell but a significant number of policyholders were not purchasing terrorism coverage by 2006. The low take-up rate was identified as a key determinant of how much capacity insurers will allocate to underwrite the risk.
- Further improvements in insurers' ability to model and manage terrorism risk would likely contribute to the long-term development of the terrorism risk insurance market. The high level of uncertainty currently associated with predicting the frequency of terrorist attacks and a general unwillingness by a significant number of insurance policyholders to purchase insurance coverage, made any prediction of the potential degree of long-term development of the terrorism risk insurance market difficult.
- Coverage for terrorism risk in group life insurance policies remained generally available and at affordable prices, despite that group life insurance has not been part of the Program.<sup>4</sup>
- Insurers generally did not provide coverage for losses resulting from CNBR events even before September 11, 2001, and for the most part were not providing CNBR coverage even with a Federal backstop in place. Given the general reluctance of insurance companies to provide coverage for these types of risks, limited capacity, relatively high prices, and policyholder expectations, there appeared to be little potential for future market development.<sup>5</sup> Subsequently, the Government Accountability Office (GAO) found that available capacity for CNBR terrorism risk insurance and reinsurance was limited.<sup>6</sup>

### **The 2008 GAO Report to Congress**

In 2008, the GAO issued a report to Congress finding that terrorism risk insurance was generally available and affordable.<sup>7</sup> Surveyed market participants and policyholders reported to the GAO that terrorism risk insurance was available nationwide and reasonably priced and affordable in current market conditions, the exception being owners of large, high value properties in major cities.<sup>8</sup> However, GAO found that those policyholders were able to adopt various approaches to obtaining terrorism coverage,

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<sup>4</sup> 2006 Report at 63.

<sup>5</sup> *Ibid.* at 72.

<sup>6</sup> GAO, Report to Congressional Committees, Terrorism Insurance – Status of Coverage Availability for Attacks Involving Nuclear, Biological, Chemical, or Radiological Weapons (GA)-09-39, Dec. 2008). In 2008, a few standalone terrorism insurers were offering standalone CNBR terrorism insurance at relatively viable prices. *See* Marsh, Terrorism Insurance Market Solutions for NBCR Exposures (2008).

<sup>7</sup> GAO, Terrorism Insurance, Status of Efforts by Policyholders to Obtain Coverage (GAO-08-1057, Sept. 2008).

<sup>8</sup> Insurers and reinsurers manage aggregation or concentration of risk by limiting the amount of coverage provided in specific areas of cities, such as downtowns and financial districts where many large buildings and businesses are clustered or other areas considered at higher risk for a terrorist attack.

*albeit* at higher rates, such as layering coverage from multiple insurers, purchasing standalone TRIA-only coverage to supplement coverage for other perils, or forming captive insurers.

### **Scope of this Report**

The 2006 Report analyzed data on the affordability and availability of terrorism risk insurance since the inception of the Program in 2002. That report identified several key factors expected to influence the market for terrorism insurance over the long-term, including the ability of insurers to measure and manage terrorism risk, and the demand for terrorism risk insurance by commercial insurance policyholders. The current Report is intended to update and supplement the 2006 Report, and should be read in conjunction with that report.

This Report focused on identifying changes in market trends since the 2006 Report and the 2007 changes to the Program. Some trends will provide important information to policymakers in re-examining the need for, or appropriate level of, a continued Federal role in the private terrorism insurance market past 2014, when the Program is set to expire. This Report comes at the near mid-point of the most recent seven-year renewal of the Program. The PWG will issue another report in 2013.

The long-term availability and affordability of terrorism risk insurance, like other goods and services, is determined by interaction between supply and demand. On the supply side, this Report examined the financial capability and willingness of insurance companies and reinsurers to allocate capacity to terrorism risk insurance. On the demand side, this Report reviewed purchase trends and alternative risk transfer by commercial insurance policyholders. As with the 2006 Report, this Report focused on *overall* market conditions while recognizing that conditions may vary by location, by sector, and by size of the insured.

### **How the PWG Conducted its Analysis**

In conducting this analysis, the PWG was assisted by staff of some of the member agencies who reviewed academic and industry studies on terrorism risk insurance. As the analysis is ongoing in nature, Treasury, as both the administrator of the Program and chair of the PWG, has been the principal monitor of developments in the marketplace.

The PWG is also required to consult with the National Association of Insurance Commissioners (“NAIC”) and others. As a means of meeting this consultation requirement in the most efficient and most transparent manner, Treasury, as chair of the PWG, published a Notice in the Federal Register seeking comments concerning the long-term availability of terrorism risk insurance. (A copy of the Federal Register Notice is included in the Appendix).<sup>9</sup> In addition to a review and analysis of the comments received from the Federal Register Notice, staff also spoke with State insurance

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<sup>9</sup> Instructions on how interested persons may review the comments received by the PWG are found in the appended Federal Register Notice (also published at 75 Fed. Reg. 34530 (June 17, 2010)).

regulators to gather further information, and also had discussions with commenters and other stakeholders.

### **Terrorism Risk Insurance Act**

The market for terrorism risk insurance since the enactment of TRIA cannot be analyzed without considering the Federal participation in the market through the Program. Accordingly, interpretation of data on market conditions and trends requires an understanding of how the Program defines the role of the Federal Government in the marketplace.

TRIA was signed into law on November 26, 2002. The stated purposes of TRIA were to address market disruptions from the terrorist attacks of September 11, 2001, to ensure the continued widespread availability and affordability of commercial property and casualty insurance for terrorism risk, and to allow for a transition period for the private markets to stabilize and build capacity while preserving State insurance regulation and consumer protections.

TRIA was established as a temporary Federal program of shared public and private compensation for privately-insured commercial property and casualty losses resulting from certified acts of terrorism. TRIA essentially amounts to a government reinsurance program in the form of a Federal backstop. Primary and excess commercial property and casualty insurers (including admitted, surplus lines, and captive insurers) that earn premiums for certain lines of commercial property and casualty insurance covering U.S. risks are required to participate in the Program.

The Department of the Treasury administers TRIA through the Program. TRIA was originally scheduled to expire on December 31, 2005, but was extended for two additional years in 2005 (with modifications), and again for seven additional years in 2007. Under current law, the Program is set to expire at the end of 2014.

### **TRIA Coverage and Limitations**

The Program covers losses only for acts of terrorism that are certified by the Secretary of the Treasury with the concurrence of the Secretary of State and the Attorney General of the United States. To qualify for certification, a terrorist act must be found to be:

- a violent act, or an act dangerous to life, property or infrastructure;
- resulting in damage within the U.S., or to a U.S. air carrier or U.S. flagged vessel, or on the premises of a U.S. mission; and
- committed by an individual or individuals as part of an effort to coerce the civilian population of the U.S. or to influence the policy or affect the conduct of the U.S. government.

Prior to the changes to the Program in 2007, only “foreign” acts of terrorism (those committed by or on behalf of foreign interests) were eligible for certification. Despite the exclusion of “domestic” acts of terrorism, the 2006 Report found that private domestic terrorism risk insurance was reportedly available and purchased within both the insurance

and reinsurance markets (not including CNBR). However, there were concerns about potential difficulty in determining whether U.S. citizens were acting on behalf of foreign interests (sometimes referred to as “homegrown” terrorists), or not (*i.e.*, “domestic” terrorists), as well as concerns about delay in certification and, in turn, coverage under the Program. As a result, TRIA was amended in 2007 to cover both domestic and foreign acts of terrorism.

In certifying an act of terrorism, some limitations apply. An act cannot be certified as an act of terrorism under TRIA if:

- the act is committed as part of a Congressionally-declared war (except that acts of war may be certified for the sole purpose of covering workers’ compensation insurance losses); or
- the property and casualty insurance losses from the act are less than \$5 million.

### **Types of Insurance Covered Under TRIA**

TRIA coverage applies to commercial property and casualty insurance. It does not apply to personal insurance, such as homeowners’, automobile, or life insurance (either individual or group life). Commercial property and casualty insurance includes excess insurance, workers’ compensation insurance, and during the first three years of the TRIA Program, surety insurance. By law, the TRIA Program does not apply to:

- Federal or private crop or livestock insurance;
- Private mortgage insurance, or title insurance;
- Financial guaranty insurance offered by a monoline financial guaranty insurance corporation;
- Insurance for medical malpractice;
- Health or life insurance, including group life insurance;
- Federal flood insurance;
- Reinsurance or retrocessional reinsurance;
- Commercial automobile insurance;
- Burglary and theft insurance;
- Surety insurance;
- Professional liability insurance; and
- Farm owners’ multiple peril insurance.

Other types of insurance were initially included in the Program but were excluded in 2005 (these include commercial automobile insurance; burglary and theft insurance; surety insurance; most professional liability insurance;<sup>10</sup> and farm owners’ multiple peril insurance).<sup>11</sup> These changes, along with increases in private sector retentions, reduced the Federal role in the terrorism risk insurance market in 2005. However, the 2007 extension of the Program did not include a similar reduction in the Federal role.

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<sup>10</sup> Directors’ and officers’ liability insurance, a type of professional liability insurance, remains in the TRIA Program. 15 U.S.C. § 6701, TRIA Section 102(12)(A).

<sup>11</sup> Terrorism Risk Insurance Extension Act of 2005, Pub. L. 109-144, 119 Stat. 2660.



Treasury, through its Program regulations, has defined the types of insurance included in the Program by “lines of insurance,” which refer to lines on regulatory financial reporting forms (*i.e.*, NAIC Annual Statement), developed by the State insurance regulators.<sup>12</sup> Insurers report premium written and earned for various types of insurance matched to the “lines.” Generally, insurance with premium that is reported on the following lines, (if not specifically excluded by law) is included in the Program: fire; allied lines; commercial multiple peril (non-liability and liability); ocean marine; inland marine; workers’ compensation; other liability;<sup>13</sup> products liability; aircraft; and boiler and machinery.

### **TRIA Requirement: Mandatory Offer of Coverage**

In general, TRIA requires that insurers “make available” coverage for acts of terrorism on the same terms and conditions as other types of coverage offered as part of their commercial property and casualty insurance policies. Insurers are not required to make coverage available for losses from a CNBR terrorist act if coverage for CNBR exposure is excluded in the overall policy, regardless of the cause of the CNBR damage (*i.e.*, the same terms and conditions).

TRIA does not require a policyholder to purchase terrorism risk insurance, although in some cases, such as with workers’ compensation insurance, State law may require such purchase. Thus, if a purchaser declines the offer of terrorism coverage, the insurer can then exclude terrorism losses from coverage under the insurance policy or negotiate other limited forms of terrorism coverage (*i.e.*, different terms and conditions than those applicable to the non-terrorism coverage).

While TRIA requires insurers to make coverage generally available, TRIA leaves pricing of terrorism risk insurance to be subject to whatever provisions may apply under applicable State law and regulation, or to the market for policies that are exempt from State rate regulation.

### **State Requirements: Mandatory Coverage**

TRIA generally preserves State insurance regulation,<sup>14</sup> and mandatory coverage depends on State law requirements applicable to admitted carriers.<sup>15</sup> For example, some States require that property insurers cover losses from fire from all causes (except war). Thus, terrorism fire and/or “fire following” an act of terrorism,<sup>16</sup> is required to be covered in at least fourteen States.<sup>17</sup> (In the remaining States, insurers must offer the coverage per

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<sup>12</sup> 31 C.F.R. Part 50, Subpart A.

<sup>13</sup> Except for professional liability insurance, which does not have a specific line. *See* 71 Fed. Reg. 50343.

<sup>14</sup> 15 U.S.C. §6701, TRIA Section 106.

<sup>15</sup> Surplus lines insurers are generally exempt from State form regulation.

<sup>16</sup> For example, since a nuclear detonation results in fire, losses from fire that follows a nuclear reaction may be covered in certain states despite the general presence of nuclear exclusions in policies.

<sup>17</sup> Twenty-eight States have laws that require commercial fire insurance policies to cover loss from fire regardless of the cause of the fire, modeled after New York’s Standard Fire Policy (these States are referred to as “Standard Fire Policy States”). Since September 11, 2001, 14 of the 28 Standard Fire Policy States have allowed fire caused by terrorism to be excluded from commercial fire policies.

TRIA). States also require that terrorism (as well as acts of war) be covered for workers' compensation, and policy exclusions are not permitted (an act of war can be certified under the Program only for workers' compensation insurance).

Even in the period between September 11 and the passage of TRIA, as insurers began excluding terrorism risk coverage from policy renewals, State insurance regulators in most States approved a terrorism exclusion for use by admitted carriers, but required that relatively small-scale terrorist attacks be covered.<sup>18</sup> However, commentators report that there has been little State law or regulatory development since 2006,<sup>19</sup> and this has been confirmed in consultation with the NAIC and State insurance regulators. Since 2006, State insurance regulators have begun collecting information from insurers regarding catastrophic events, including acts of terrorism, as some States have begun a more risk-based focus examination of insurer solvency. This information will help regulators learn of insurers' probable maximum loss, how risk concentrations are determined, and the use of reinsurance and capital market products to spread the risk of catastrophic losses. The NAIC explained that such information collection recently has begun and the collected data will be helpful going forward.

### **Insurers' Retention of Losses under TRIA**

The Program involves shared public and private compensation for privately-insured commercial property and casualty losses resulting from acts of terrorism. The private sector insurers' share of the losses has several components: (1) the insurer deductible; (2) the insurer share of insured losses above the deductible; (3) a floor loss threshold before the Federal Government shares in the losses; (4) a ceiling loss threshold through an annual cap on aggregate insured losses paid under the Program; and (5) an insurance marketplace aggregate retention which establishes a minimum amount of aggregate insured losses that will be borne by private industry, both commercial insurance policyholders and insurance companies. These elements, described in further detail below, combine as the insurers' annual retention of insured losses and the insurers' loss limit within which the market operates.

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<sup>18</sup> The exclusion most States approved for admitted carriers generally provided that terrorism resulting in total losses of less than \$25 million or where no more than 50 people were injured (a relatively small-scale attack) could not be excluded (except for CNBR events).

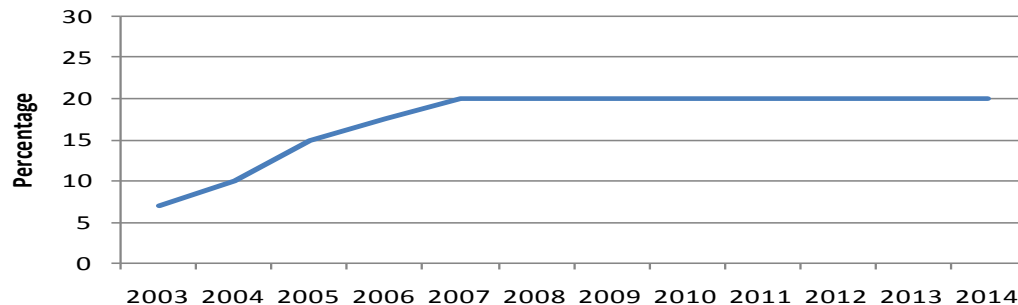
<sup>19</sup> Swiss Re suggests that one action States could take to improve affordability of terrorism insurance risk is to make the coverage mandatory for all thereby spreading the risk across the largest possible base of insured. Comments by Swiss Re to the PWG (Aug. 2, 2010). *See also*, OECD, Conference on Terrorism Risk Insurance, Improving Existing Solutions (June 2010).

## 1. Insurer Deductible

If a certified terrorist act occurs, insurers may be eligible to receive the Federal Government's share of the insured losses above a deductible, as specified under TRIA. Insurance companies will cover 100 percent of the insured losses below their deductible. An insurer's TRIA deductible remains constant no matter how much terrorism risk insurance coverage it sells because the deductible is calculated as a percentage of the previous year's direct earned premiums (DEP) from covered lines of commercial property and casualty insurance, not just terrorism insurance. Many insurance companies, including captive insurers, reinsure some portion of their insurer deductible.

For the initial period of the temporary three-year Program, and through the Program's first extension, the insurer deductible percentage increased gradually each year, but remained fixed starting in 2007. The insurer deductible, as a percentage of the prior year's direct earned premiums, rose from 7 percent in 2003, to 10 percent in 2004, 15 percent in 2005, 17.5 percent in 2006, and 20 percent in 2007 (though in 2006 and 2007 there were fewer lines of insurance in the TRIA Program from which the deductible was calculated). However, the percentage was fixed at 20 percent starting in 2007, and is set to remain at 20 percent through 2014.

### Insurer Deductible Percentage of Prior Year Direct Earned Premiums



Source: TRIA

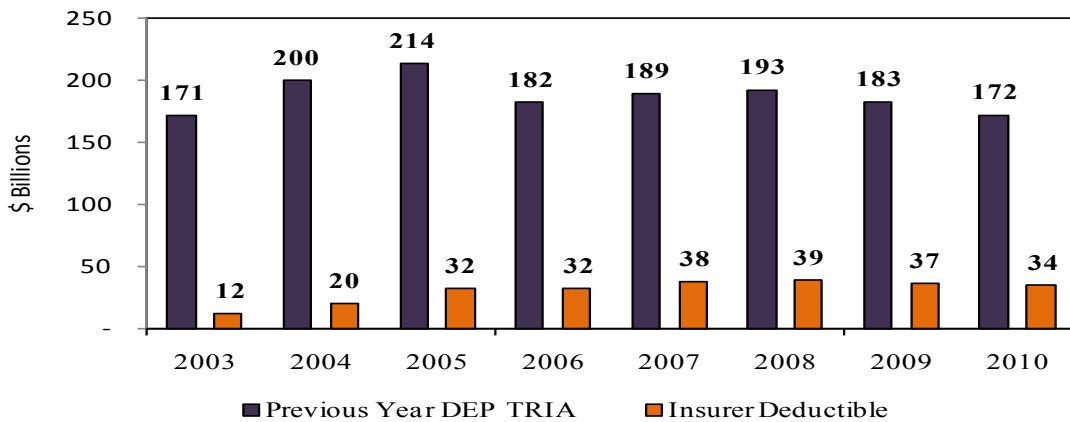
Insurers are not required to report their annual insurer deductibles to either regulators or the Program, but will be required to do so if a claim for Federal payment is made to the Program.<sup>20</sup> While individual insurer deductibles will vary based on their lines of business and premium volumes,<sup>21</sup> it is nevertheless useful to examine the trend in insurer retention based on aggregate DEP data in TRIA lines.

<sup>20</sup> 31 C.F.R. Part 50, Subpart F.

<sup>21</sup> A large insurance company reported that its DEP in TRIA lines and insurer deductible has remained stable. Comments by The Hartford to the PWG dated 2010. Another, the Liberty Mutual Group reports an increase in its insurer deductibles from 2006 to 2010. Comments by the Liberty Mutual Group to the PWG (Aug. 2, 2010).

The chart below shows the trends in aggregate insurer deductibles based on DEP in TRIA lines. According to data from A.M. Best, the aggregate insurer deductibles climbed from \$12 billion in 2003 to \$32 billion in 2005, due to both an increase in DEP and the insurer deductible percentage. The aggregate insurer deductible leveled off in 2006 as the number of lines covered by TRIA declined between 2005 and 2006. DEP in TRIA lines has decreased since 2007, and the aggregate insurer deductible (fixed at 20 percent of the prior year's DEP), has dropped from approximately \$38 billion to \$34 billion.<sup>22</sup> Based on expectations of a “soft” market and further downward pressure on commercial property and casualty prices, aggregate insurer deductible may continue to decrease,<sup>23</sup> although the DEP and deductibles could increase if market conditions firm.<sup>24</sup>

**Previous Year Direct Earned Premiums (DEP) in TRIA Lines and Aggregate Insurer Deductible**



Source: Treasury

<sup>22</sup> Data was compiled from Best's Aggregates and Averages, Property and Casualty, 2003 – 2009 editions. DEP data includes all premium reported in lines included in the Program, which may include some premium earned from insurance be excluded by TRIA but reported within the line. Insurers are required to not include those premiums in their deductible calculation under the Program's claims regulations. As a result, for purposes of this analysis, aggregate premium may be overstated somewhat. The American Academy of Actuaries identified the same downward trend from 2006 to 2010 and found that the aggregate insurer deductible decreased by 1.4 percent from 2006 to 2007, increased by 1 percent from 2007 to 2008, dropped by 5 percent from 2008 to 2009, and dropped by another 6 percent from 2009 to 2010. See Comments by the American Academy of Actuaries to the PWG (Aug. 2, 2010). Aon also found that the aggregate insurer deductible increased by 1.2 percent from 2007 to 2008 (\$33.7 billion to \$34 billion), declined by 4.5 percent in 2009 (\$32.6 billion) and dropped another 6 percent in 2010 (\$30.6 billion). See Comments by the Aon Corporation to the PWG (Aug. 2, 2010). A similar analysis by an insurance trade association also found similar decreases from 2008 to 2010. See Comments by the Property and Casualty Insurers of America to the PWG (2010).

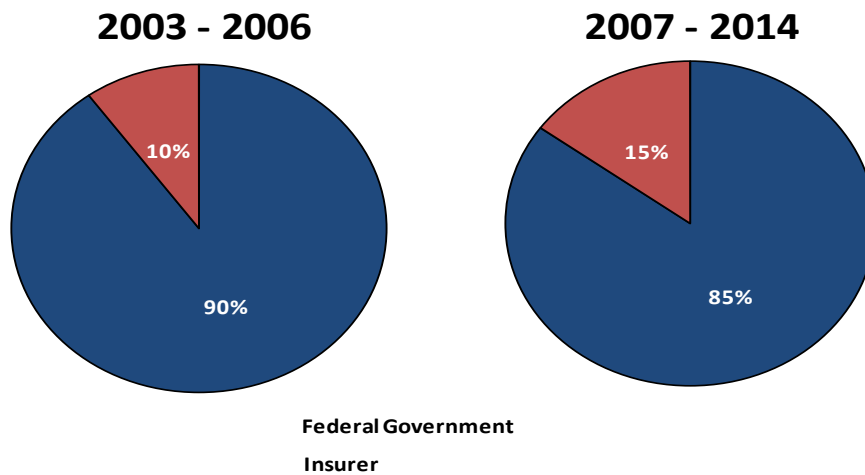
<sup>23</sup> Soft market conditions generally refer to periods in which premium rates are stable or falling and insurance is readily available. Hard market conditions are where rates rise, coverage may be more difficult to find.

<sup>24</sup> Comments by the National Association of Mutual Insurance Companies to the PWG (Aug. 2, 2010).

## 2. *Insurer Share of Losses Above the Deductible*

Under the Program, insured losses above the insurer deductible amount are shared between the insurance company and the Federal Government. As TRIA was originally enacted, the insurer share was fixed at 10 percent of the insured losses, and the Federal Government's share equal to 90 percent of the losses above the deductible. When the Program was extended in 2005, the insurer share was raised to 15 percent in 2007, reducing the Federal share slightly to 85 percent. Under current law, the public and private shares remain at these levels through 2014.

### Insurer and Federal Share Losses Above Insurer Deductible



Source: TRIA

## 3. *The Program Trigger of Federal Payments*

TRIA mandates certain limitations on Federal payments under the Program. The Terrorism Risk Insurance Extension Act of 2005<sup>25</sup> amended TRIA so the Federal Government would not share in the losses of relatively small-scale acts of terrorism. TRIA prohibits the Program from making Federal payments until the aggregate industry insured losses resulting from a certified act of terrorism exceed the "Program Trigger," which was first set at \$50 million in 2006 and increased to \$100 million in 2007, where it is set to remain for the duration of the Program. Acts of terrorism above \$5 million in aggregate insured losses remain eligible for certification under the Program, and any certification will trigger coverage under terrorism risk insurance policies. However, the Federal Government does not share in any losses until the Program Trigger is reached. The Program Trigger, therefore, serves as a floor on Federal payments under the Program. Below that floor, the private sector retains all of the losses.

<sup>25</sup> Pub. L. 109-144, 119 Stat. 2660.

#### 4. Annual Cap on Public and Private Payment under the Program

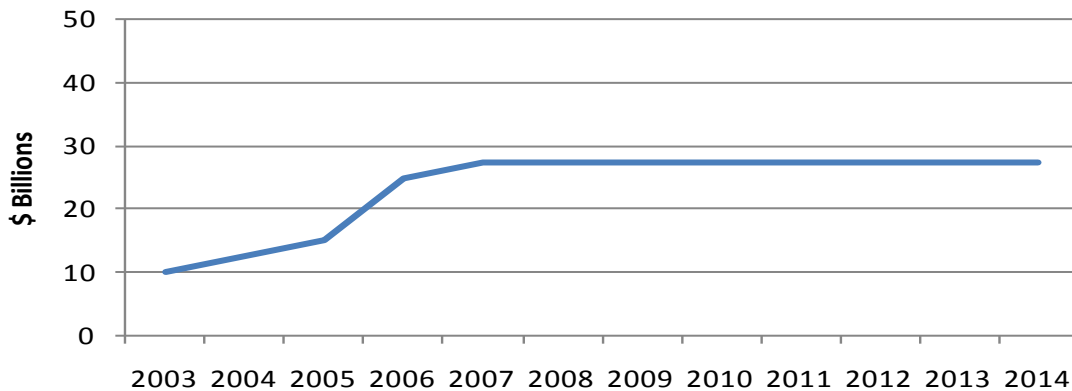
Another limitation on payments involves what is referred to as the Program’s “cap” on annual liability. Under TRIA, neither the Federal Government, nor private insurers who have paid losses at least up to their insurer deductible, will be liable for any amount exceeding an annual cap of \$100 billion in aggregate insured losses.<sup>26</sup> TRIA provides that Treasury must notify Congress that the cap has been reached. This cap has not been increased since the Program was enacted.

#### 5. Recoupment of the Federal Share of Insured Losses and the Marketplace Aggregate Retention

TRIA does not require participating insurers to pay premiums up front, rather, it is post-loss funded. TRIA provides authority for Treasury to recoup its Federal payments *via* surcharges on commercial insurance policyholders. A certain amount of recoupment is mandatory, based on insurance marketplace aggregate annual retention amounts specified in TRIA. In other situations, however, TRIA authorizes discretionary recoupment.

The recoupment requirement ensures that the private sector, on an aggregate basis, retains at least a minimum amount of the insured losses. As shown in the figure below, the insurance marketplace aggregate retention amount began at \$10 billion in 2003 and gradually increased to \$12.5 billion (2004); \$15 billion (2005), \$25 billion (2006); and \$27.5 billion (2007). When the Program was extended in 2007, the marketplace retention was left at the 2007 level through 2014.

### Insurance Marketplace Aggregate Retention Amount

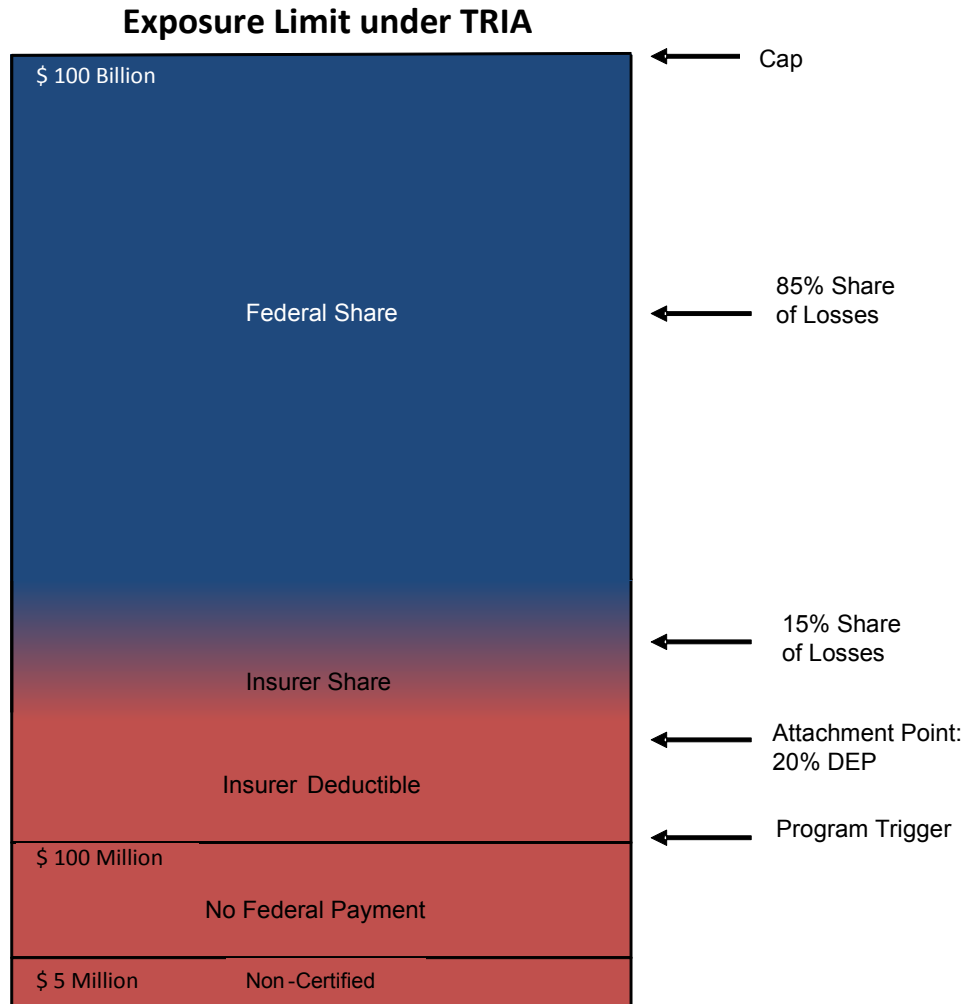


Source: TRIA

<sup>26</sup> 15 U.S.C. §6701, TRIA Section 103(e)(2).

## TRIA and the Market

The parameters of the TRIA Program, including the insurer deductible; insurer share of losses; Program Trigger; cap; and the marketplace aggregate retention, define and limit the exposure to losses within which the insurance market currently operates. The Program allows insurers to manage exposure within the defined parameters of the insurer deductible and the insurers' 15 percent share of the losses.<sup>27</sup> The Program provides an exposure limit, as illustrated below:



## Loss Experience

To date, no certified acts of terrorism have occurred under the Program; commercial insurance policyholders have suffered no losses; and insurers have incurred no claims. As a result, there have been no Federal payments under the Program and no policyholder surcharges (either mandatory or discretionary) have been assessed.

<sup>27</sup> Comments by the Liberty Mutual Group to the PWG (2010).

Although there have been no Federal payments under the Program, there have been administrative costs. In addition, TRIA creates an unfunded contingent liability of the Federal Government and, as such, the Program increases the Federal budget deficit.<sup>28</sup> The Federal budget outlay represents a subsidy estimate: the expected cost borne by Federal taxpayers due to the program.

### **Policyholder Surplus Has Increased**

The availability of terrorism risk insurance is affected by insurer capital. Insurance company capital is measured by net worth (assets less liabilities), referred to as policyholder surplus, and is the amount of risk capital available to underwrite and assume risk. Policyholder surplus is a measure of underwriting capacity because it reflects the financial resources that stand behind every insurance policy written.<sup>29</sup> The amount of capital maintained dictates the amount of insurance an insurer is able to issue, including terrorism or other perils. Accordingly, capacity to underwrite terrorism risk insurance, or the amount allocated to that risk, is partly a function of the available capital of the property and casualty industry as a whole, and of insurance companies individually.

The chart below shows policyholder surplus for the property and casualty industry over the last decade. According to NAIC data, after September 11, 2001, combined policyholder surplus of property and casualty insurers dropped to an estimated \$302 billion by the end of 2002. Between 2002 and 2006, industry surplus steadily climbed, reaching \$508 billion in 2006, reflecting recovery from the effects of the September 11 attacks as well as a rebound in the stock market (among other things).<sup>30</sup> The recovery of the industry was seen as a favorable development toward facilitating the long-term availability and affordability of terrorism risk insurance going forward.

Policyholder surplus continued to rise to \$551 billion in 2007, but dipped to \$493 billion in 2008, most likely attributable to the decrease in earnings and valuation of insurers' assets from the global economic crisis; however, surplus rebounded and reached \$556 billion in 2009.<sup>31</sup> Overall, this surplus should facilitate the provision of terrorism coverage.

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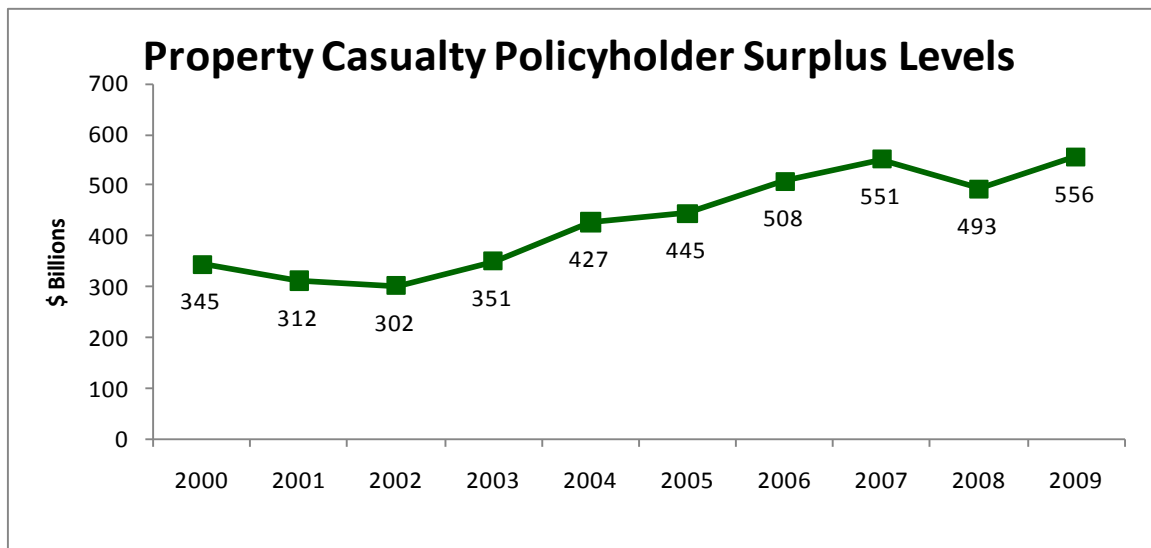
<sup>28</sup> Office of Management and Budget (OMB), Budget of the U.S. Government, Fiscal Year 2010; Congressional Budget Office (CBO), Federal Reinsurance for Terrorism Risks: Issues in Reauthorization (Aug. 2007).

<sup>29</sup> Insurance Information Institute, Financial Market Conditions (May 2010).

<sup>30</sup> 2006 Report at 31-33.

<sup>31</sup> A.M. Best estimated policyholder surplus at \$532 billion among the top 100 property and casualty insurers. A.M. Best, Best's Statistical Study, U.S. Property/Casualty 2009 Policyholder Surplus (Nov. 15, 2010).





Source: NAIC<sup>32</sup>

### **Insurers Appear Willing to Provide More Terrorism Risk Insurance; Capacity Has Increased**

In insurance parlance, capacity refers to the total amount of exposure to loss that an insurance or reinsurance company is willing to assume from a peril. One measure used for estimating market capacity is to aggregate the maximum amount of coverage an insurer is willing to provide to any one insured (called “per risk” capacity). Such an analysis presents a theoretical maximum of available capacity. The theoretical maximum represents the total available capacity if terrorism risk insurance were purchased from all available insurers at the maximum level each insurer is willing to underwrite. Commercial insurance policyholders, however, do not purchase at these maximum levels; policy limits are well below the theoretical maximum. Nevertheless, the theoretical maximum is a useful metric of market capacity.

There have been several reports of increased availability and capacity of terrorism risk insurance, including:

- The Aon Corporation, a large insurance and reinsurance broker, reports significant increases in terrorism risk coverage under “all risk”,<sup>33</sup> or all perils, property insurance policies.<sup>34</sup> A theoretical maximum of \$13.5 billion per risk is currently available, up from a maximum of about \$8 billion reported in 2005.<sup>35</sup>

<sup>32</sup> NAIC, Statistical Compilation of Annual Statement Information for Property/Casualty Insurance Companies in 2009 (2010).

<sup>33</sup> An “all risk” commercial property insurance policy usually provides coverage against all risks of physical loss or damage to the property insured except to the extent a particular risk is excluded from the policy coverage through exclusions in the policy.

<sup>34</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>35</sup> *Ibid.*

- A significant increase in capacity is also reported in the standalone market.<sup>36</sup> Aon reports a remarkable 67 percent increase in standalone capacity from 2006 to 2010. Available capacity aggregated from standalone insurers grew from approximately \$1.5 billion in 2006 to over \$2.5 billion, with a potential upper bound of \$3.8 billion in 2010.<sup>37</sup>
- Marsh, another large insurance broker, reports that standalone capacity has increased by approximately 65 percent since 2006. Standalone capacity in the fourth quarter of 2006, on an aggregate basis, was between approximately \$1.1 billion to \$2.3 billion.<sup>38</sup> In the first quarter 2007, capacity increased to between approximately \$1.3 billion to \$2.5 billion.<sup>39</sup> By the first quarter 2009, capacity climbed to \$3.1 billion<sup>40</sup>, and by the second quarter, \$3.76 billion.<sup>41</sup> Marsh reports that capacity is now at approximately \$3.8 billion.<sup>42</sup>
- Marsh attributes the increase in capacity since 2007 to an increase in insurer willingness to underwrite more standalone coverage and additional capacity from new entrants to the market, even in a competitive price environment. Aon also reports that standalone capacity has emerged from existing market participants allocating more capacity, as well as from new market entrants, including new and expanded capacity from Lloyd's of London syndicates.<sup>43</sup> Lloyd's reports that favorable loss experience (*i.e.*, no terrorism claims), combined with the enhanced ability to manage and model exposure with reinsurance support, has attracted new capacity.<sup>44</sup>
- Capacity depends on risk and location. Marsh reports that, generally, capacity increases significantly outside of commercial business districts. Approximately \$750 million to \$2 billion, per risk, in standalone terrorism insurance capacity is available for companies that do not have sizeable exposure in locations where insurers face aggregation challenges. Capacity in excess of \$2 billion is available but at higher premiums. For others, in locations where standalone insurers have aggregate exposure concentrations, estimated capacity is at approximately \$850 million to \$1 billion.<sup>45</sup>

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<sup>36</sup> Standalone terrorism insurance policies, as their name implies, cover terrorism risk alone, and are an alternative to obtaining terrorism risk insurance coverage as part of an insured's "all risk" policy. Standalone policies compete on price and terms. Standalone coverage can also provide excess coverage above "all risk" coverage limits or can fill "gaps" in coverage, such as by covering losses as a result of non-certified acts of terrorism or at non-US locations (*i.e.*, non-TRIA coverage). Standalone insurers also assume reinsurance of captive insurers' TRIA deductibles.

<sup>37</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>38</sup> Marsh, Marketwatch: Terrorism Insurance 2006, The Standalone Terrorism Market (Dec. 2006).

<sup>39</sup> Marsh, Marketwatch: Terrorism Insurance 2007, The Standalone Terrorism Market (April 2007).

<sup>40</sup> Marsh, Marketwatch: Terrorism Insurance 2009, The Standalone Terrorism Market (1Q 2009).

<sup>41</sup> Marsh, Marketwatch: Terrorism Insurance 2010, The Standalone Terrorism Market (2Q 2010); The Marsh Report: Terrorism Risk Insurance 2010.

<sup>42</sup> Marsh, The Marsh Report: Terrorism Risk Insurance 2010 (2010).

<sup>43</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>44</sup> Comments by Lloyd's of London to the PWG (Aug. 2, 2010).

<sup>45</sup> Marsh, Marketwatch: Terrorism Insurance 2010, The Standalone Terrorism Market (2Q 2010).

- While overall capacity has increased, there remain challenges in some markets. Capacity is restricted for certain iconic buildings, sports stadiums, entertainment theme parks and transportation hubs.<sup>46</sup> Aon reports that capacity is restricted in Chicago, New York City, and San Francisco.<sup>47</sup> Some corporate insurance policyholders in high-risk urban areas still have difficulty obtaining coverage with sufficient limits.<sup>48</sup> Lloyd's confirms that capacity is constrained for large property exposures and in certain locations, such as Manhattan.<sup>49</sup>

Capacity, the amount of available risk capital that an insurance company may be willing to allocate to a particular risk or location, is tied to its ability to measure and manage accumulations or concentrations of risk to determine its maximum loss under different scenarios. The increases in capacity reported above have occurred with reports of improvement in models used by insurers.

### **Modeling and Insurer Management of Aggregate Exposure**

The 2006 Report explained that insurers were developing modeling techniques to manage risk exposure and make decisions as to allocated capacity and price.<sup>50</sup> Models were being developed and used to measure an insurer's aggregate loss exposure by estimating the damage from a predetermined event of a certain magnitude and at a specific location as measured against the number of policies and limits written in the target area. Probabilistic models were being developed to predict frequency and severity. The 2006 Report explained that improvements in industry data collection and modeling would improve insurer management of aggregate exposure and lead to increased capacity for terrorism risk insurance.<sup>51</sup> The American Academy of Actuaries claim that modeling to measure an insurer's aggregate loss exposure based on predetermined attack scenarios has improved since 2006.<sup>52</sup>

Lloyd's explains there have been significant advances within the insurance industry as data collection has been standardized improving the quality, consistency, and accuracy of information.<sup>53</sup> Aon confirms that there have been substantial improvements since 2006 in terms of the ability of insurers and reinsurers to assess and manage aggregate terrorism accumulation exposures.<sup>54</sup> The Hartford reports that its ability to measure and manage accumulations for terrorism risk has improved through the use of internal and external models that have improved over time.<sup>55</sup> Much has been learned in nine years of managing and assessing terrorism risk, and tools have been developed. The standalone market has become specialized and has the most experience in managing terrorism aggregate exposures. Improved risk management has led to a nominal increase in

<sup>46</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>47</sup> *Ibid.*

<sup>48</sup> Comments by the American Bankers Insurance Association (Aug. 2, 2010).

<sup>49</sup> Comments by Lloyd's of London to the PWG (Aug. 2, 2010).

<sup>50</sup> Insurers use modeling to match risk to price and to determine how much aggregate to assume. Insurance Information Institute, Financial Market Conditions (May 2010).

<sup>51</sup> 2006 Report at 23.

<sup>52</sup> Comments by the American Academy of Actuaries to the PWG (Aug. 2, 2010).

<sup>53</sup> Comments by Lloyd's of London to the PWG (Aug. 2, 2010).

<sup>54</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>55</sup> Comments by The Hartford to the PWG dated 2010.

capacity.<sup>56</sup> While capacity remains constrained in dense urban centers with large commercial insurance concentrations (*e.g.*, Manhattan, Washington, D.C., Los Angeles, and San Francisco), improvements in aggregate monitoring technology have reportedly increased capacity in these areas.<sup>57</sup>

Since 2006, the improved ability of insurers to measure aggregate exposure has led rating agencies to consider terrorism exposure in assessing the capital adequacy of insurers. The views of rating companies can be influential on the amount of capacity insurers decide to allocate to terrorism risk insurance.<sup>58</sup> The 2006 Report discussed A.M. Best's Supplemental Rating Questionnaire (SRQ) in which risk accumulations/concentrations and aggregate exposure were surveyed. In 2008, A.M. Best added a new Terror Probable Maximum Loss capital charge to the Best's Capital Adequacy Ratio, as part of its rating methodology.<sup>59</sup> In 2006, S&P also began surveying insurers<sup>60</sup> to assess terrorism exposure as part of a company's enterprise risk management.<sup>61</sup> Although these are noteworthy developments in the marketplace, it may be difficult to assess the impact rating company methodologies may have on insurer capacity decisions as many factors affect a company's rating.

Despite the reported improvements in modeling to measure an insurer's aggregate loss exposure, the industry remains uncertain about the reliability of probabilistic models to predict frequency and severity of terrorist attacks. According to Aon, the ability to accurately model terrorism risk in terms of frequency and severity is a key factor in the decision by insurers and reinsurers as to how much capacity to allocate to the risk.<sup>62</sup> Probabilistic models have been updated with new research and information to improve the estimation of frequency and severity.<sup>63</sup> Yet, probabilistic models are viewed as having limited value in predicting frequency and severity of conventional and CNBR terrorist acts and are limited in addressing attacks on multiple targets in multiple locations ("swarm attacks").<sup>64</sup> The American Insurance Association ("AIA") reports that modeling firms have made little progress in predicting frequency over the last 9 years.<sup>65</sup> Aon states that there appears to have been little improvement in frequency assessment.<sup>66</sup>

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<sup>56</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>57</sup> *Ibid.*

<sup>58</sup> GAO, Terrorism Insurance, Status of Efforts by Policyholders to Obtain Coverage (GAO-08-1057, Sept. 2008).

<sup>59</sup> A.M. Best, The Treatment of Terrorism Risk in the Rating Evaluation (Sept. 2, 2009); A.M. Best, Understanding BCAR for Property/Casualty.

<sup>60</sup> Insurance Journal, S&P Alters Approach to Gauging Insurers' Terrorism Exposure (June 8, 2006).

<sup>61</sup> See generally, Standard & Poors, Expanded Definition of Adequate Classification in Enterprise Risk Management Scores (2010).

<sup>62</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>63</sup> Comments by the American Academy of Actuaries to the PWG (Aug. 2, 2010).

<sup>64</sup> Comments by The Hartford to the PWG dated 2010.

<sup>65</sup> Comments by the American Insurance Association to the PWG (Aug. 2, 2010).

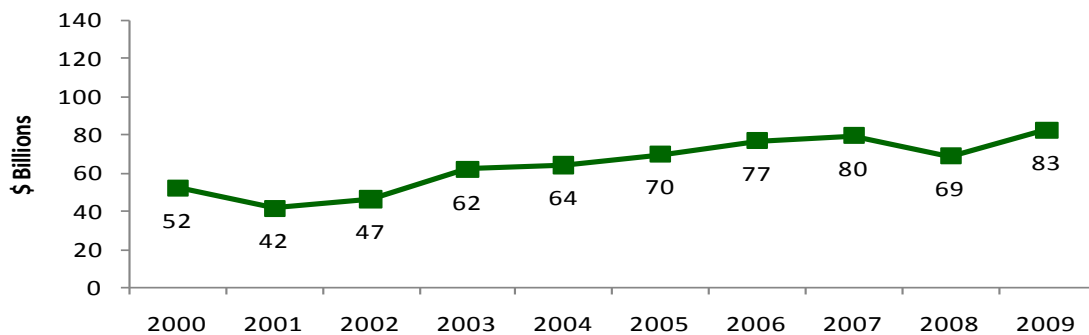
<sup>66</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

## Reinsurer Capital Has Increased

Reinsurance continues to play an important role in the availability of terrorism risk insurance. The transfer of terrorism risk from insurer to reinsurer frees up capital, which becomes available to underwrite more insurance. Insurer capacity increases as reinsurance capacity increases and is purchased.

Similar to primary insurance, capacity to reinsure risk is affected by the available capital of reinsurers. The available capital of major U.S. property and casualty reinsurers generally has increased since 2001. As shown on the chart below, reinsurers' surplus was approximately \$83 billion at the end of 2009.

### Reinsurers' Policyholder Surplus Levels



Source: RAA<sup>67</sup>

## Reinsurers Are Not Allocating More Capital; Capacity Has Remained Stable or Increased Slightly

Although it is difficult to measure available reinsurance capacity, there does not seem to have been a measurable increase in recent years. In 2006, a Reinsurance Association of America (“RAA”) survey indicated that reinsurance capacity available in the U.S. for terrorism risk was between \$6 and \$8 billion in aggregate, up from \$4 to \$6 billion in 2005.<sup>68</sup> Based on the RAA’s most recent survey of reinsurance brokers and underwriters, “the global reinsurance capacity available in the United States for terrorism risk has increased only slightly since 2006 and likely remains in the \$6-8 billion range.” Marsh commented that it does not believe that reinsurers are allocating any more capacity to terrorism risk insurance than they did in 2006.<sup>69</sup> The AIA and others agree.<sup>70</sup> Aon states that it does not believe reinsurance capacity exceeds \$8 to \$10 billion.<sup>71</sup>

<sup>67</sup> RAA, Reinsurance Underwriting Review, A Financial Review of U.S. Reinsurers, 2009 Industry Results (2010).

<sup>68</sup> 2006 Report at 26.

<sup>69</sup> Comments by Marsh to the PWG (Aug. 2, 2010).

<sup>70</sup> Comments by the American Insurance Association to the PWG (Aug. 2, 2010); Comments by the Financial Services Roundtable to the PWG (Aug. 2, 2010).

<sup>71</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

One large insurance company commented that terrorism risk reinsurance has developed modestly but that it remains insufficient to serve the market's current risk exposure in the absence of the Program given that it is only a small fraction of reinsurance industry capital.<sup>72</sup> As a whole, insurers are retaining roughly 80 percent of the risk although individual insurance company retention and reinsurance levels vary.

RAA explains that reinsurers have grown slightly more comfortable with terrorism reinsurance and the slight increase in capacity along with technological advances in modeling aggregate exposure have driven prices down. Marsh also explains that reinsurers better understand the risk and are using models in pricing reinsurance, although models are viewed as being limited in predicting frequency of attacks.<sup>73</sup> Still, the RAA points out that the inability to assign frequencies to occurrence affects demand for coverage.

### **Reinsurance Capacity from Other Sources Has Not Developed**

The 2006 Report suggested that capital market sources might provide additional terrorism reinsurance.<sup>74</sup> However, the AIA explains that despite some growth in the market for catastrophe ("cat") bonds for natural catastrophe risks, such vehicles have not been used to transfer terrorism risk to the capital markets.<sup>75</sup> A large insurance company confirms that there is no active securitization market for terrorism risk and the likelihood that such will develop is remote given the limitations in modeling frequency and severity, and thus in the rating of the bonds.<sup>76</sup>

### **Insurers Are Not Purchasing More Reinsurance, Even at Lower Prices**

The 2006 Report pointed out that the amount of reinsurance capacity allocated to terrorism risk also depends to some degree on the willingness of insurers to purchase reinsurance.<sup>77</sup> Insurers generally make decisions to purchase reinsurance based on perception of risk, price, and comfort with the retention of risk exposures. The RAA recently described this market behavior:

Typical insurance and reinsurance cycles involve temporary increases in pricing, followed by new market participants, leading to increased competition and price moderation. Reinsurance is a sophisticated business decision for insurers and their reinsurance costs are impacted by how much and at what layers they buy it, if at all, within their financial model for handling risk.<sup>78</sup>

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<sup>72</sup> Comments by The Hartford to the PWG (2010).

<sup>73</sup> Comments by Marsh to the PWG (Aug. 2, 2010); Higher prices might attract more capacity, Lloyd's explains, but capital allocation is impeded by the inability to calculate event probability. *See* Comments by Lloyd's of London to the PWG dated August 2, 2010.

<sup>74</sup> 2006 Report at 26-27.

<sup>75</sup> Comments by the American Insurance Association to the PWG dated August 2, 2010.

<sup>76</sup> Comments by The Hartford to the PWG (2010); Comments by the American Academy of Actuaries to the PWG (Aug. 2, 2010).

<sup>77</sup> 2006 Report at pp. 27-31.

<sup>78</sup> RAA, *State of the Reinsurance Market 2009*.

In 2006, it appeared that insurers were not willing to purchase available reinsurance,<sup>79</sup> and that appears to remain true today. There have been a number of reports that insurers are not purchasing reinsurance despite lower reported pricing. These include:

- In June 2010, Marsh released a report, *Terrorism – Reinsurers Standing By*, stating that global and U.S. reinsurance purchase and pricing levels have generally fallen from the peak period following September 11 (2002-2004).<sup>80</sup> This market behavior is consistent with that seen with other low frequency, high severity risks following the passage of time without a large loss event. However, as prices have fallen, insurers are not purchasing available reinsurance. As Marsh observes: “[o]n the surface, it would seem that lower pricing over time would increase activity [purchase] levels, but interestingly we see simultaneous lower prices and lower activity levels.” In the U.S. market, “activity levels are clearly down.”
- According to a cited survey of reinsurance underwriters by Guy Carpenter & Company, LLC (a Marsh affiliate), 83 percent of reinsurers are actively seeking new or expanded terrorism reinsurance business. Standalone treaty business has decreased over time, particularly in the U.S. market.<sup>81</sup> Reinsurers are even more willing to provide CNBR reinsurance coverage and capacity has increased, although price for CNBR coverage is still a factor.
- The RAA reports that reinsurance capacity exceeds demand in the standalone reinsurance market.<sup>82</sup> Pricing for terrorism reinsurance decreased in 2007-2008 by about 50 percent. CNBR reinsurance capacity exists but on a very limited basis and at a significant premium. (According to Swiss Re, reinsurance for CNBR events is estimated at only \$1 to \$2 billion).<sup>83</sup>
- Aon also reports that supply exceeds demand in the standalone terrorism reinsurance market. Increased capacity and advances in modeling have driven prices down. Still, the inability to predict probability and frequency affects buyer (insurer) perception of terrorism risk and decisions to forego purchasing reinsurance.<sup>84</sup>
- Aon reports that standalone reinsurance purchased on an aggregate, all lines basis, has fallen 50 percent in the last 18 to 24 months, from high-teen percentage rates on line (ROL) to high-single digit percentage ROL for the coverage, including for CNBR.<sup>85</sup>
- Lloyd’s underwriters report that standalone reinsurance capacity from the Lloyd’s of London market has grown since 2006.<sup>86</sup> This has been due to improvements in risk

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<sup>79</sup> 2006 Report at 27.

<sup>80</sup> MMC, *Terrorism – Reinsurers Standing By* (June 2010); *see also* Marsh Comments to the PWG (2010).

<sup>81</sup> Reinsurance contracts take the form of either standalone or multi-peril treaties with reinsurers preferring standalone terrorism risk contracts.

<sup>82</sup> Comments by the Reinsurance Association of America to the PWG (July 29, 2010).

<sup>83</sup> Comments by Swiss Re to the PWG (Aug. 2, 2010).

<sup>84</sup> Comments by Aon to the PWG (Aug. 2, 2010).

<sup>85</sup> Rate on line (ROL) refers to the price of reinsurance as a percentage applied against the loss or policy limits offered by the contract or policy.

mapping, accumulation management, and in measuring potential severity of losses. However, probabilistic modeling of the frequency and severity of a terrorist attack remains a challenge.<sup>87</sup>

- Lloyd's reports that the price of reinsurance has fallen due to the increase in capacity in the market in general and at Lloyd's, and the lack of recent terrorism losses in the U.S. Insurers are willing to pay the current market price for terrorism risk insurance but underwriters believe that the price has fallen to a level below the true economic value of the risk and therefore further growth in capacity is unlikely. At current price levels, Lloyd's expects capacity to retract in coming years.
- According to the RAA, aggregate reinsurance limits, on an all lines basis, is available in the \$300 to \$400 million range, inclusive of coverage for CNBR. Excluding CNBR, limits are available perhaps as much as \$1 billion, but are not often purchased at such levels. According to Aon, up to \$1 billion in coverage is available per risk in non-metropolitan areas (exclusive of CNBR cover), and up to \$400 million in metropolitan areas. If CNBR coverage is included, available per risk capacity drops to \$100 million. Per risk capacity has increased in the last 24 months. Capacity has increased due to expanded entry into this market from insurers otherwise writing direct standalone coverage. According to Aon, reinsurance on an aggregate, all lines basis is available up to \$350 to \$400 million including CNBR and up to \$1 billion excluding CNBR.<sup>88</sup>
- Marsh believes that capacity is available in the range of \$700 million depending on location and other factors. Marsh estimates that \$700 million is available on a per-occurrence basis, up to \$1 billion.<sup>89</sup> More than \$1 billion of workers' compensation reinsurance may be available.<sup>90</sup>
- In terms of pricing, Marsh reports that the cost of terrorism reinsurance is driven primarily by the location of the risks being reinsured. Standalone terrorism reinsurance is available at a cost roughly equal to 1 to 4 percent of the reinsurance limit in less-risky locations. In targeted cities and densely populated commercial areas, the cost can be as much as 10 to 20 percent of the limit purchased. Reinsurance for workers' compensation is more available and at a lower cost than property risks, even in high-risk areas.<sup>91</sup>

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<sup>86</sup> Capacity in both property reinsurance treaties, and workers' compensation (and employers' liability) contracts, has generally not changed since 2006.

<sup>87</sup> Comments by Lloyd's of London to the PWG dated August 2, 2010.

<sup>88</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>89</sup> Comments by Marsh to the PWG (Aug. 2, 2010).

<sup>90</sup> MMC, Terrorism – Reinsurers Standing By (June 2010).

<sup>91</sup> Comments by Marsh to the PWG (Aug. 2, 2010).

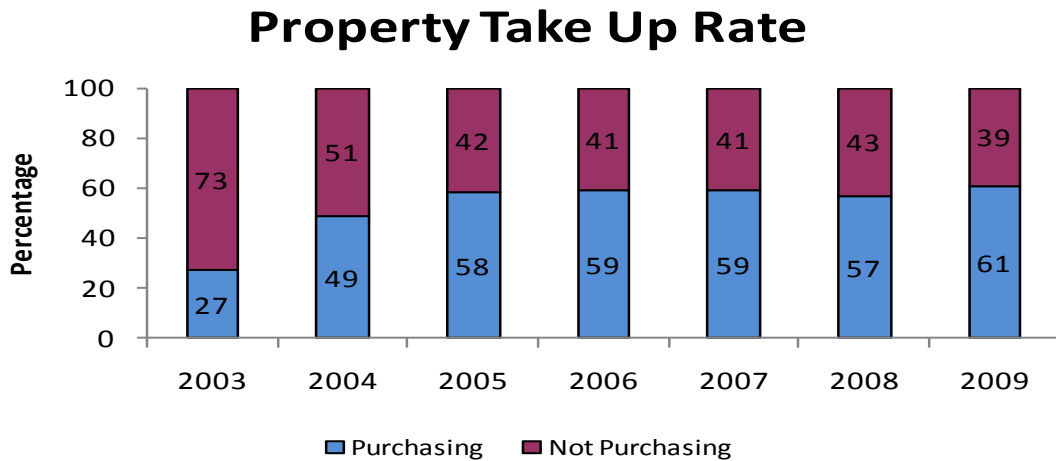


## Take-Up Rate of Terrorism Risk Insurance Has Levelled

TRIA requires that insurers “make available” coverage for acts of terrorism on the same terms and conditions as other types of coverage offered as part of their commercial property and casualty insurance policies. TRIA does not mandate the purchase of terrorism risk insurance. The decision by policyholders to accept or reject the offer and to insure or retain terrorism risk remains generally voluntary.<sup>92</sup>

The general trend observed in 2006 was that of year-to-year increases in the number of policyholders purchasing terrorism risk insurance.<sup>93</sup> Since 2006, the number of policyholders purchasing terrorism risk insurance appears to have steadied, even as prices for those purchasing coverage have continued to fall. Commercial insurance agents and brokers report that policyholder demand seems to have reached a plateau in recent years.<sup>94</sup>

A number of studies and reports have presented information on policyholder take-up rates. For example, Marsh reports that, since the enactment of TRIA, property take-up rates, in general, increased from 30 to 60 percent with the rate remaining around 60 percent between 2006 and 2009.<sup>95</sup>



Source: Marsh<sup>96</sup>

<sup>92</sup> State law may mandate purchase. For example, most States require most employers purchase workers' compensation insurance, which covers acts of terrorism. The market may compel purchase decisions, such as by lenders as a condition of financing.

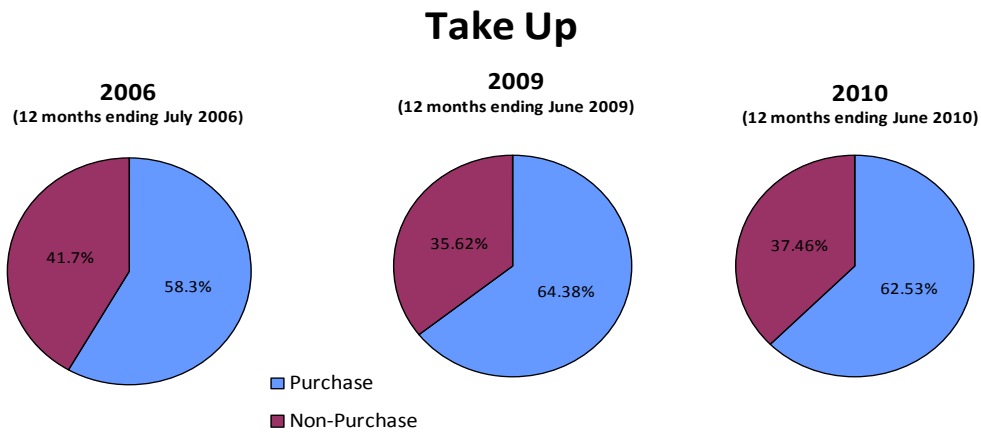
<sup>93</sup> 2006 Report at 42.

<sup>94</sup> Comments by the Council of Insurance Agents and Brokers to the PWG (Aug. 2, 2010).

<sup>95</sup> In its 2010 Marketwatch report, Marsh states that approximately 90 percent of its clients purchased terrorism risk insurance as part of their property policies rather than as standalone policies.

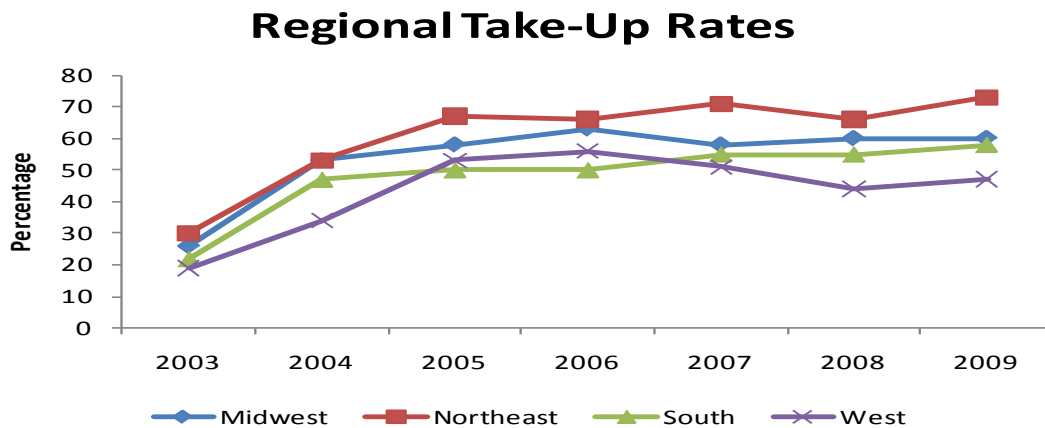
<sup>96</sup> The Marsh Report: Terrorism Risk Insurance 2010.

According to data from Aon, take-up rates for all types of terrorism coverage (standalone and part of property policies) increased from 58.3 percent in 2006<sup>97</sup> to just under 65 percent in 2009 and 2010 (see chart).<sup>98</sup>



Take-up rates have also been tracked by region, size of company (by insured value), and commercial insurance policyholder sector. Reports and studies have presented the following:

- Regionally, as tracked by Marsh, take-up rates have historically been highest in the Northeast – currently 73 percent, up from 66 percent in 2006. Take-up has decreased slightly in the Midwest from 63 percent in 2006 to 60 percent in 2009, while it has increased in the South from 50 percent to 58 percent. Take-up in the West dropped from 56 percent in 2006 to 47 percent in 2009.



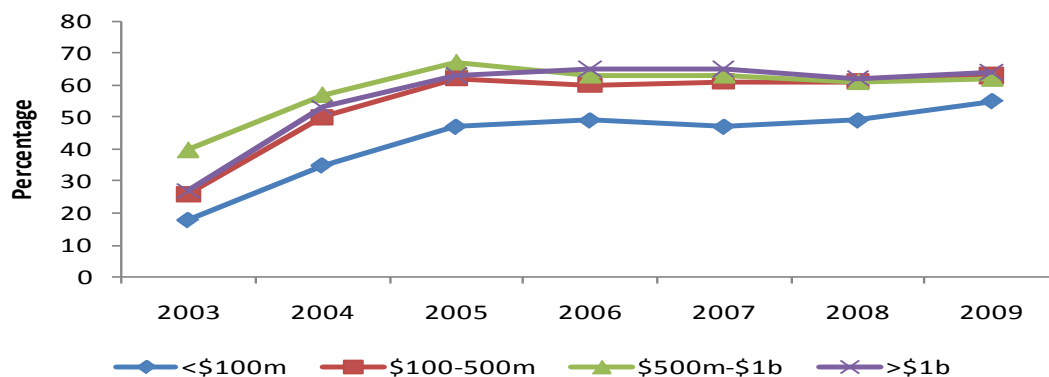
<sup>97</sup> Aon data provided to the PWG in 2006.

<sup>98</sup> Aon data provided to the PWG in 2010.

<sup>99</sup> The Marsh Report: Terrorism Risk Insurance 2010; Marketwatch: Terrorism Insurance – 2006 Market Conditions and Analysis.

- Marsh also tracks take-up rates by company size, as measured by the company's total insured value (TIV). As shown in the chart below, take up rates generally increase somewhat with company size: In 2009, smaller companies with TIV below \$100 million had the lowest take up rate at 55 percent, while larger companies had take up rates in the range of 62 to 64 percent. The largest companies, those with TIV over \$1 billion had the highest take up rate (64 percent), and were more likely to use captive insurers to manage terrorism risk.

### Take-Up by Company Size



Source: Marsh<sup>100</sup>

- In the second quarter of 2010, take-up of Aon's large property clients was at 61 percent, down slightly from 63 percent in 2009.<sup>101</sup>
- Take-up rates by sector are shown in the table below. According to Marsh, the real estate, health care, transportation, financial institutions, and media sectors had take-up rates above 70 percent in 2009. From 2006 to 2009, take-up has been steady, except for increases in the public and transportation sectors, and drops in financial institutions and education, as shown in the chart below (peak take-up in red).

Sector	2003 %	2004 %	2005 %	2006 %	2007 %	2008 %	2009 %	Percentage Change 06-09
Utility	27	42	65	77	81	73	80	3.90
Real Estate	30	60	79	77	80	73	76	-1.30
Health Care	31	60	76	76	71	75	76	0.00
Transportation	30	41	66	51	62	64	75	47.06
Financial Institutions	27	65	79	81	73	68	74	-8.64
Media	35	58	74	68	64	71	71	4.41
Hospitality	32	48	69	66	69	67	68	3.03
Education	22	54	65	76	71	69	65	-14.47
Technology/Telecom	43	43	61	59	63	61	61	3.39
Public Entity	26	42	56	55	61	55	61	10.91
Retail	20	48	51	59	58	54	60	1.69
Construction	--	23	43	45	47	49	52	15.56
Manufacturing	18	38	43	43	45	43	47	9.30
Food & Beverage	35	39	64	57	51	53	42	-26.32
Energy	41	36	45	57	66	62	40	-29.82

Source: Marsh<sup>102</sup>

<sup>100</sup> The Marsh Report: Terrorism Risk Insurance 2010; Marketwatch: Terrorism Insurance – 2006 Market Conditions and Analysis.

<sup>101</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

Aon has also tracked take-up by the way terrorism risk insurance coverage is purchased. Terrorism risk insurance falls into 4 categories: (1) “TRIA only,” which refers to U.S. locations and certified act coverage as backstopped by the Program, and as part of an “all risk” property insurance policy; (2) “TRIA and Non-Certified,” which refers to both certified and non-certified (U.S. and non-U.S. locations) coverage as part of a property policy; (3) “standalone,” which refers to a standalone policy not part of property coverage which covers U.S. and non-U.S. locations and TRIA and non-TRIA events<sup>103</sup>; and (4) “TRIA and Standalone,” which refers to a combination of coverage through property policies and standalone policies.

<b>Take Up by Coverage Type</b>	<b>2006 (12 mos. ending April 2006)<sup>104</sup></b>	<b>2009 (12 mos. ending June 2009)<sup>105</sup></b>	<b>2010 (12 mos. ending March 2010)<sup>106</sup></b>
Not Purchased	40.5	35.31	38.5
Standalone	4.5	6.87	8.42
TRIA & Non-certified	43.6	47.33	37.10
TRIA & Standalone	3.7	2.1	2.15
TRIA only	7.6	8.4	13.8

- According to the table shown above, take-up rates appear to have leveled off with 40 percent of commercial businesses electing to remain uninsured. The decline of “TRIA & Non-certified” and increase of “TRIA only” coverage corresponds to the 2007 inclusion of domestic terrorism in the Program.

### **Captives Continue to Provide Coverage**

Another manner in which businesses secure terrorism risk insurance is through captive insurers. A single-parent captive is a limited-purpose, wholly owned subsidiary that can be used to insure the captive’s parent or affiliates. Captives are expected to have smaller insurer deductibles as compared to traditional insurers since DEP in TRIA lines is likely to be small.<sup>107</sup> Captives, with low insurer deductibles, can be a less expensive and attractive alternative for large or high-risk policyholders.<sup>108</sup>

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<sup>102</sup> The Marsh Report: Terrorism Risk Insurance 2010; Marketwatch: Terrorism Insurance – 2006 Market Conditions and Analysis; Marketwatch: Terrorism Insurance 2005, Focus: Private Equity and Mergers and Acquisitions.

<sup>103</sup> Standalone policies are generally purchased by clients with sizable target exposures not met by the all risk property market.

<sup>104</sup> Aon 2006 Property Report, A Tale of Two Markets (2006).

<sup>105</sup> Aon data presented to PWG in 2010.

<sup>106</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>107</sup> Marsh, Captives, TRIA, and Standalone Terrorism Reinsurance Solutions (March 2007). In 2007, the Program was changed with a Program Trigger which prohibits the Federal Government from sharing in any losses unless the aggregate industry insured losses resulting for a certified act of terrorism exceed \$100 million. As a result, captives may require additional capital or reinsurance protection increasing the cost of coverage.

<sup>108</sup> Comments by the American Insurance Association to the PWG (Aug. 2, 2010).

Marsh reports that more companies are securing coverage through captives and purchasing reinsurance to cover their insurer retentions under the Program.<sup>109</sup> Commercial insurance policyholders report that, in addition to providing lower-cost alternatives to insurance from traditional insurers, captives provide excess insurance; as well as primary coverage not provided by traditional insurers, such as losses from CNBR events and cyber-attacks.<sup>110</sup> Captives are providing CNBR coverage in large metropolitan areas, such as New York City, Chicago, San Francisco, Boston, and Washington, D.C.<sup>111</sup> An association of captive insurers estimates that there are now more than 100 terrorism-specific captives and many more that provide terrorism coverage along with other lines of insurance (*e.g.*, property, workers' compensation, and general liability).<sup>112</sup>

### **Policyholders Appear to Be Purchasing Higher Amounts of Coverage**

Among those commercial insurance policyholders taking up terrorism risk insurance, there is some indication that more coverage, as measured by policy limits, may be being purchased.

<b>Median Policy Limits by Coverage Type (Millions of Dollars)</b>		
<b>Coverage Type</b>	<b>2005</b>	<b>2009-2010</b>
Standalone	\$50	\$250
TRIA & Non-certified	\$225	\$258
TRIA & Standalone	\$400	\$577
TRIA only	\$100	\$200

Source: Aon

According to data reported by Aon, median policy limits have increased since 2005 across all types of terrorism coverage. Commercial insurance policyholders purchasing insurance covering TRIA certified acts and non-certified acts in 2009-2010 purchased median limits of \$258 million,<sup>113</sup> up from median limits of \$225 million in 2005.<sup>114</sup> Median policy limits among those purchasing TRIA only coverage rose from \$100 million in 2005 to \$200 million in 2009-2010, while median limits among those purchasing a combination of coverage through property policies and standalone policies reportedly rose from \$400 million in 2005 to \$577 million in 2009-2010.<sup>115</sup> For standalone coverage only, median limits among Aon clients reportedly rose fivefold, from \$50 million in 2005 to \$250 million in 2009-2010.

<sup>109</sup> Comments by Marsh to the PWG (Aug. 2, 2010).

<sup>110</sup> Comments by the Coalition to Insure Against Terrorism to the PWG (Aug. 2, 2010).

<sup>111</sup> Comments by the Captive Insurance Companies Association to the PWG (July 30, 2010).

<sup>112</sup> Comments by the Vermont Captive Insurance Association to the PWG (Aug. 2, 2010). Vermont is a leading captive insurer domicile.

<sup>113</sup> Aon data submitted to the PWG; for averages, *see* Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>114</sup> Aon, Property Terrorism Update, TRIA in the Balance (2005).

<sup>115</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

## Terrorism Risk Insurance Premiums Have Declined

Data reported in 2006 demonstrated general declines or stability in terrorism risk insurance pricing. Since then, prices have reportedly continued to decline. Aon reports a progressive downward trend in terrorism risk insurance pricing – both for U.S. and non-U.S. risks.<sup>116</sup> Aon reports that overall, pricing has declined 30 percent (plus) from 2006 to the first quarter 2010, continuing a downward trend that began in 2003.<sup>117</sup> Aon expects rates overall to decrease 10 percent through 2010. Marsh reports that the cost of terrorism risk insurance has fallen gradually year-to-year, with a more significant drop in 2009.<sup>118</sup> The Lloyd's of London market (Lloyd's) also reports that since 2006 there has been a continued downward trend in terrorism risk insurance prices.<sup>119</sup> With no major losses, prices continue to decline. The exception is in high-risk locations where price has remained more stable.<sup>120</sup>

Policyholders report experiencing declines in terrorism risk insurance pricing with the exception of high-risk areas where capacity is limited and pricing more expensive, such as New York City, Chicago, San Francisco, Boston, and Washington, D.C.<sup>121</sup> In comments to the PWG, one group of commercial insurance policyholders reports general declines in pricing for terrorism risk insurance.<sup>122</sup> From the policyholder perspective, terrorism risk insurance has become more affordable.

The most common measures used for evaluating pricing trends for terrorism risk insurance are based on tracking surveys conducted by insurance agents and brokers. Since the inception of the Program, pricing has been surveyed and tracked as (1) a percentage of a policyholder's total insured value (TIV); (2) percentage of overall property insurance premium; and (3) percentage of price change quarter-by-quarter. Reports indicate that terrorism risk insurance premiums have declined since the establishment of the Program as well as since 2006.

One caveat in interpreting these data on pricing is that we only observe prices on market transactions for those who purchase insurance coverage, we do not observe offer prices for all commercial insurance policyholders. As a result, we are limited in our ability to draw conclusions about demand for terrorism coverage among those not purchasing coverage.

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<sup>116</sup> *Ibid.* Aon reports that pricing was not affected by the addition of domestic terrorism to the Program in 2007 and pricing has continued to trend downward.

<sup>117</sup> *Ibid.*

<sup>118</sup> Comments by Marsh to the PWG (Aug. 2, 2010).

<sup>119</sup> Comments by Lloyd's of London to the PWG (Aug. 2, 2010). Lloyd's underwriters provide terrorism risk insurance as surplus lines insurers. The majority of the terrorism coverage coming from the Lloyd's market is written on a standalone basis.

<sup>120</sup> Comments by Lloyd's of London to the PWG (Aug. 2, 2010).

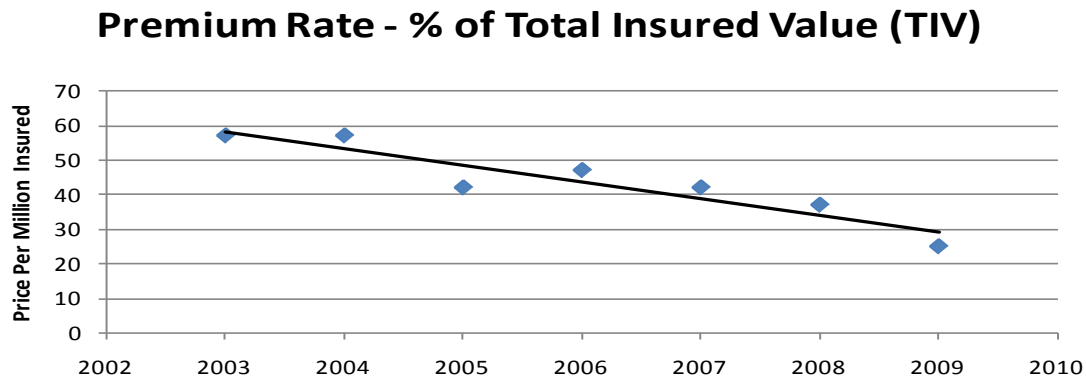
<sup>121</sup> Comments by the Risk and Insurance Management Society, Inc., to the PWG (2010).

<sup>122</sup> Comments by the Coalition to Insure Against Terrorism to the PWG (Aug. 2, 2010).

## Terrorism Premium as Percent of Total Insured Value (TIV)

A number of sources have compiled data indicating that premiums, as measured as a percentage of TIV, are declining for terrorism coverage included as part of broader “all risk” property policies and when provided on a standalone basis. Examples include:

- Marsh reports that terrorism insurance premiums overall decreased from \$56 per million of insured value in 2004 to \$47 per million in 2006. Between 2006 and 2009, premiums declined 53 percent to \$26 per million of insured value.



Source: Marsh<sup>123</sup>

- While overall premium rates have declined over the past two years, these declines were experienced only by smaller companies; rates for larger companies have actually remained stable or increased slightly. For companies with TIV of less than \$100 million, the premium was \$53 per million of insured value in 2009, down slightly from \$54 per million in 2008. For companies with TIV of between \$100 and \$500 million TIV, premiums fell from a median of \$36 per million of insured value in 2008 to \$32 per million in 2009. For those between \$500 million and \$1 billion, there was an increase from \$27 per million of insured value in 2008 to \$29 per million in 2009.<sup>124</sup> For companies with TIV over \$1 billion, premiums remained at \$27 per million.
- Marsh found that by industry, median premium rates decreased for 11 of 15 sectors between 2008 and 2009. Premiums increased for real estate (\$42 to \$56 per million); hospitality (\$54 to \$55 per million); and technology/telecommunication (\$24 to \$29 per million); and remained steady for retail (\$26 per million).<sup>125</sup> Rates dropped for construction (\$76 to \$65 per million); utilities (\$59 to \$51 per million); financial institutions (\$62 to \$47 per million); and transportation (\$74 to \$46 per million).<sup>126</sup>

<sup>123</sup> The Marsh Report: Terrorism Risk Insurance 2010; Marketwatch: Terrorism Insurance – 2006 Market Conditions and Analysis; Marketwatch: Terrorism Insurance 2006.

<sup>124</sup> The Marsh Report: Terrorism Risk Insurance 2010.

<sup>125</sup> The Marsh Report: Terrorism Risk Insurance 2010.

<sup>126</sup> *Ibid.*

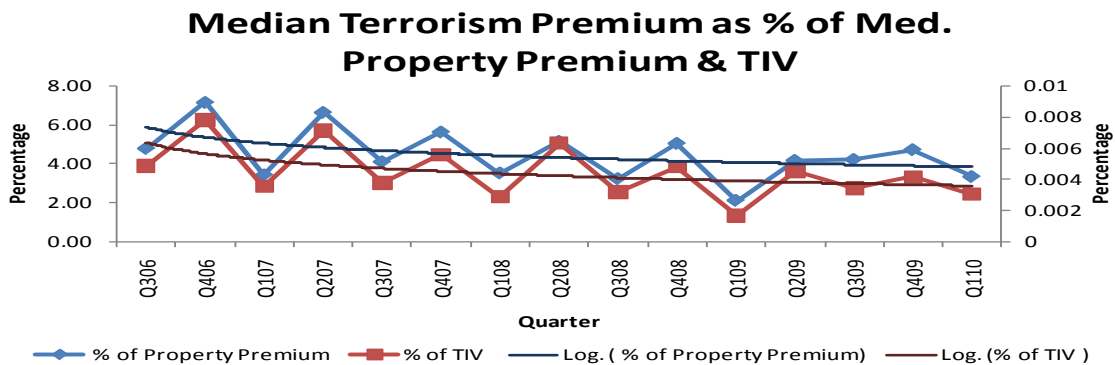
- According to Marsh, median rates have dropped across all regions between 2006 and 2009. In the Midwest, rates fell significantly from \$38 per million of insured value in 2006 to \$21 in 2009; in the Northeast, from \$57 to \$36 per million; in the South, \$54 to \$38 per million; and in the West, from \$54 to \$30.<sup>127</sup>
- Standalone pricing, as a percent of TIV, has dropped to 0.0096 percent from 2006 when Aon reported that rates then ranged from 0.025 percent to 1 percent.<sup>128</sup>

### Terrorism Premium as Percentage of Overall Property Premium

Premiums for terrorism risk insurance included as part of “all risk” property insurance policies have decreased. Commercial insurance agents and brokers explain that the soft market has had some effect on this pricing since competition has driven prices down for all types of insurance.<sup>129</sup> Aon also notes that terrorism risk insurance pricing is tied to the overall property and casualty pricing trends and soft market conditions.<sup>130</sup> During the last few years, soft market conditions have resulted in general price declines in property and casualty insurance overall, not just terrorism risk insurance. Downward pressure on pricing has been attributed to excess capacity, increased competition, economic conditions facing buyers, and other factors.<sup>131</sup>

Data leading up to the 2006 Report suggested that terrorism risk insurance premiums measured as a percentage of overall premiums decreased following September 11, 2001.<sup>132</sup> This trend has continued.

- Aon data shows pricing declines as measured both as a percentage of TIV and percentage of overall property insurance premium.



Source: Aon

<sup>127</sup> The Marsh Report: Terrorism Risk Insurance 2010; Marketwatch: Terrorism Insurance – 2006 Market Conditions and Analysis.

<sup>128</sup> Comments by the Aon Corporation to the PWG (Apr. 21, 2006).

<sup>129</sup> Comments by the Council of Insurance Agents and Brokers to the PWG (Aug. 2, 2010).

<sup>130</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>131</sup> A.M. Best, Best’s Special Report, U.S. P/C Industry Profits First-Quarter Profit Despite Surge in Catastrophes (July 8, 2010); Best’s Special Report, Surplus Lines Drained, Not Dry, From Soft Market Economy (Sept. 27, 2010).

<sup>132</sup> 2006 Report at 36.

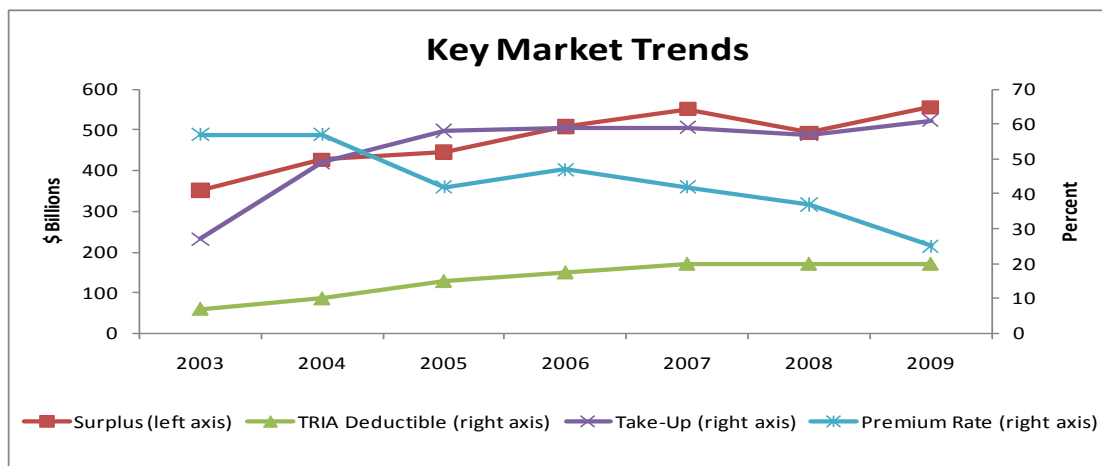


- Standalone terrorism risk insurance pricing has also declined.<sup>133</sup> The soft market in property insurance market leads to expectations of lower price by purchasers of standalone policies.<sup>134</sup>

However, for some commercial insurance policyholders, as a percentage of overall premium, terrorism premium is taking a larger share of the insurance budget; for others, the percentage remained stable or fell. Reports include:

- According to Marsh, for companies with TIV of less than \$100 million, the terrorism premium as a percentage of overall premium rose from 4 percent in 2007 to 22 percent in 2009. For companies with TIV of between \$100 and \$500 million, the percentage fell from 14 percent in 2007 to 5 percent in 2009. The percentage remained relatively stable for companies between \$500 million and \$1 billion, from 6 percent in 2007 to 7 percent in 2009. There was an increase from 8 percent to 11 percent for companies with over \$1 billion in TIV.<sup>135</sup>
- For some industry sectors, terrorism premium is commanding more of the overall insurance premium. For financial institutions, the percentage jumped from 14 percent in 2008 to 24 percent in 2009, having been at 8 percent in 2006. For the transportation sector, the percent rose from 11 percent in 2008 to 17 percent in 2009, up from 4 percent in 2006. Real estate increased from 5 percent in 2006 and 6 percent in 2008 to now 10 percent in 2009. For other sectors, the terrorism premium as a percentage of overall premium has remained relatively stable, although hospitality saw a drop from 13 percent in 2008 to 4 percent in 2009 and the energy and food-and-beverage sectors had modest declines.<sup>136</sup>

## Key Market Trends and Conclusion



<sup>133</sup> Comments by the Aon Corporation to the PWG (Aug. 2, 2010).

<sup>134</sup> Comments by Lloyd's of London to the PWG (Aug. 2, 2010).

<sup>135</sup> The Marsh Report: Terrorism Risk Insurance 2010.

<sup>136</sup> *Ibid.*; Marketwatch: Terrorism Insurance – 2006 Market Conditions and Analysis.

The key factors examined in this Report regarding the long-term availability and affordability of terrorism risk insurance centered around indicators of capacity and demand for coverage. In summary, since 2006: insurer and reinsurance capacity has increased; policyholder take-up has leveled off; purchase of reinsurance has dropped; and prices of terrorism risk insurance and reinsurance have generally fallen. A key trend is that private sector capacity for terrorism risk insurance has continued to increase, as demand, insurers' retention, and the Federal Government's role have all held steady.

Overall, a number of positive market conditions appear to have emerged since 2006:

- Insurers reportedly continue to further improve their ability to manage terrorism risk and to model the measurement of an insurer's aggregate loss exposure;
- The financial condition of the property and casualty insurance and reinsurance industry has improved;
- Terrorism risk insurance capacity has increased significantly, particularly in the standalone market; and
- Generally, prices continue to decline for both terrorism risk insurance and reinsurance.

There are other conditions that will also continue to be monitored:

- The ability to predict the frequency and severity of acts of terrorism is likely to remain a key challenge long-term;
- Policyholder take-up is at the 60 percent level, without any significant change since 2006.
- Buyer demand for coverage seems to have leveled off despite falling prices among those who purchase insurance, leaving a good portion of businesses – some 40 percent – uninsured;
- Although challenges remain for some (*i.e.*, high value properties, high-risk businesses or locations), terrorism risk insurance is available; and
- Insurer retentions have stabilized under the Program.

Given the nature of terrorism, probabilistic models have limited potential to address the uncertainty associated with predicting the frequency and severity of terrorist attacks. This may limit further development of reinsurance capacity.

Some 40 percent of businesses are not purchasing terrorism risk insurance coverage, even as prices continue to fall for those purchasing coverage. For this segment of the market, this suggests that the demand for terrorism coverage may be less sensitive to price,<sup>137</sup> or that potential buyers may perceive their risk to be lower than that which is priced into

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<sup>137</sup> One academic scholar points to “major concerns as to whether 4 out of 10 corporations in the U.S. that declined TRIA coverage would have the capacity to sustain a large scale terrorist attack if it happened tomorrow (they are typically the smaller ones in our sample).” Michel-Kerjan, Erwann, *Corporate Demand for Terrorism Insurance: An Empirical Analysis* (June 2010). Corporate demand for catastrophic insurance, such as terrorism risk insurance, is found to be more premium inelastic (*i.e.*, less sensitive to price) than for non-catastrophic insurance. *Ibid.*

available terrorism coverage. At any rate, take-up of terrorism coverage appears to have leveled off at 60 percent.

As many commenters point out, the Program provides incentive to property and casualty insurers and reinsurers who might not otherwise provide terrorism risk insurance at current capacity levels, or at current prices, absent Federal support or State law mandates. It does this by providing some degree of certainty of an insurers' maximum loss exposure. However, policymakers should review aspects of the Program in order to encourage further development by the private sector.

The PWG will continue to analyze market conditions, as required by TRIA, and report to the Congress in 2013.

## **APPENDIX**

Building Ground Floor, Room W12-140, 1200 New Jersey Avenue, SE., Washington, DC 20590. You may also send comments electronically via the Internet at <http://www.regulations.gov/smses.dot.gov/submit/>. All comments will become part of this docket and will be available for inspection and copying at the above address between 10 a.m. and 5 p.m., E.T., Monday through Friday, except federal holidays. An electronic version of this document and all documents entered into this docket is available on the World Wide Web at <http://www.regulations.gov>.

**FOR FURTHER INFORMATION CONTACT:** Joann Spittle, U.S. Department of Transportation, Maritime Administration, 1200 New Jersey Avenue, SE., Room W21-203, Washington, DC 20590. Telephone 202-366-5979.

**SUPPLEMENTARY INFORMATION:** As described by the applicant the intended service of the vessel CEST LA VIE is:

*Intended Commercial Use of Vessel:* "Vessel Chartering Operations."  
*Geographic Region:* "Intended operations will be the west coast of the U.S. California, Oregon, and Washington."

#### Privacy Act

Anyone is able to search the electronic form of all comments received into any of our dockets by the name of the individual submitting the comment (or signing the comment, if submitted on behalf of an association, business, labor union, etc.). You may review DOT's complete Privacy Act Statement in the **Federal Register** published on April 11, 2000 (Volume 65, Number 70; Pages 19477-78).

By Order of the Maritime Administrator.  
Dated: June 11, 2010.

**Julie P. Agarwal,**

*Acting Secretary, Maritime Administration.*

[FR Doc. 2010-14688 Filed 6-16-10; 8:45 am]

**BILLING CODE 4910-81-P**

## DEPARTMENT OF TRANSPORTATION

### Surface Transportation Board

[Docket No. FD 35371]

#### Nittany & Bald Eagle Railroad Company—Temporary Trackage Rights Exemption—Norfolk Southern Railway Company

Norfolk Southern Railway Company (NSR), pursuant to a written trackage rights agreement dated April 13, 2010, has agreed to grant nonexclusive overhead temporary trackage rights to Nittany & Bald Eagle Railroad Company

(N&BE), between Lock Haven and Driftwood, Pa., from milepost BR 194.2 to milepost BR 139.2, a distance of approximately 55 miles.<sup>1</sup>

The transaction may be consummated on or after July 1, 2010, and the temporary trackage rights are scheduled to expire on December 15, 2010. The purpose of the temporary trackage rights is to allow N&BE adequate bridge train service for temporary, seasonal traffic originating on the N&BE for delivery to an off-line destination.

As a condition to this exemption, any employees affected by the acquisition of the temporary trackage rights will be protected by the conditions imposed in *Norfolk and Western Railway—Trackage Rights—Burlington Northern, Inc.*, 354 I.C.C. 605 (1978), as modified in *Mendocino Coast Railway—Lease and Operate—California Western Railroad*, 360 I.C.C. 653 (1980), and any employees affected by the discontinuance of those trackage rights will be protected by the conditions set out in *Oregon Short Line Railroad and The Union Pacific Railroad Company—Abandonment—Portion Goshen Branch Between Firth and Ammon, in Bingham and Bonneville Counties, Idaho*, 360 I.C.C. 91 (1979).

This notice is filed under 49 CFR 1180.2(d)(8). If it contains false or misleading information, the exemption is void *ab initio*. Petitions to revoke the exemption under 49 U.S.C. 10502(d) may be filed at any time. The filing of a petition to revoke will not automatically stay the transaction. Petitions for stay must be filed no later than June 24, 2010 (at least 7 days before the exemption becomes effective).

An original and 10 copies of all pleadings, referring to Docket No. FD 35371, must be filed with the Surface Transportation Board, 395 E Street, SW., Washington, DC 20423-0001. In addition, a copy of each pleading must be served on Richard R. Wilson, 518 N. Center Street, Suite 1, Ebensburg, PA 15931.

Board decisions and notices are available on our Web site at "<http://www.stb.dot.gov>."

Decided: June 14, 2010.

<sup>1</sup> A redacted, executed trackage rights agreement between NSR and N&BE was filed with the notice of exemption. The unredacted version was concurrently filed under seal along with a motion for protective order, which will be addressed in a separate decision.

By the Board, Rachel D. Campbell,  
Director, Office of Proceedings.

**Kulunie L. Cannon,**  
*Clearance Clerk.*

[FR Doc. 2010-14664 Filed 6-16-10; 8:45 am]

**BILLING CODE 4915-01-P**

## DEPARTMENT OF THE TREASURY

### Analysis by the President's Working Group on Financial Markets on the Long-Term Availability and Affordability of Insurance for Terrorism Risk

**AGENCY:** Departmental Offices, Department of the Treasury.

**ACTION:** Notice; request for comments.

**SUMMARY:** The Terrorism Risk Insurance Act of 2002 (Pub. L. 107-297, 116 Stat. 2322), as amended by the Terrorism Risk Insurance Program Reauthorization Act of 2007 (Pub. L. 110-160, 121 Stat. 1839), requires the President's Working Group on Financial Markets to perform an on-going analysis regarding the long-term availability and affordability of insurance for terrorism risk.

The President's Working Group on Financial Markets (established by Executive Order 12631) is comprised of the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, the Chairman of the Securities and Exchange Commission, and the Chairman of the Commodity Futures Trading Commission (or their designees). The Secretary of the Treasury, or his designee, is the Chairman of the President's Working Group on Financial Markets. As chair of the President's Working Group on Financial Markets, Treasury is issuing this Notice for public comment to assist the President's Working Group with its analysis.

**DATES:** Comments must be in writing and received by August 2, 2010.

**ADDRESSES:** Please submit comments electronically through the Federal eRulemaking Portal: <http://www.regulations.gov>, or by mail (if hard copy, preferably an original and two copies) to Treasury's Office of Financial Institutions Policy, Attention: President's Working Group on Financial Markets Public Comment Record, Room 1417 MT, Department of the Treasury, 1500 Pennsylvania Avenue, NW., Washington, DC 20220. Because postal mail may be subject to processing delay, it is recommended that comments be submitted electronically. All comments should be captioned with "President's Working Group on Financial Markets: Terrorism Risk Insurance Analysis."

Please include your name, affiliation, address, e-mail address and telephone number(s) in your comment. Where appropriate, comments should include a short Executive Summary (no more than five single-spaced pages).

In general, comments received will be posted on <http://www.regulations.gov> without change, including any business or personal information provided. Comments received, including attachments and other supporting materials, are part of the public record and subject to public disclosure. Do not enclose any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure. In addition, all comments received will be available for public inspection by appointment at the Reading Room of the Treasury Library. To make appointments, please call the number below.

**FOR FURTHER INFORMATION CONTACT:** C. Christopher Ledoux, Acting Director, Office of Financial Institutions Policy, 202-622-2730 (not a toll free number).

**SUPPLEMENTARY INFORMATION:** The Terrorism Risk Insurance Act of 2002 (Pub. L. 107-297, 116 Stat. 2322) (hereinafter referenced as "TRIA") was enacted on November 26, 2002. TRIA's purposes are to address market disruptions, to ensure the continued widespread availability and affordability of commercial property and casualty insurance for terrorism risk, and to allow for a transition period for the private markets to stabilize and build capacity while preserving State insurance regulation and consumer protections. Title I of TRIA established a temporary Federal program of shared public and private compensation for insured commercial property and casualty losses resulting from an act of terrorism, as defined in the Act. TRIA authorized Treasury to administer and implement the Terrorism Risk Insurance Program (hereinafter referenced as the "Program"), including the issuance of regulations and procedures.

As originally enacted, the Program was to end on December 31, 2005; however, on December 22, 2005, the Terrorism Risk Insurance Extension Act of 2005 (Pub. L. 109-144, 119 Stat. 2660) was enacted, which extended the Program through December 31, 2007. On December 26, 2007, the Terrorism Risk Insurance Program Reauthorization Act of 2007 (Pub. L. 110-160, 121 Stat. 1839) was enacted, which extended the Program through December 31, 2014.

Section 108(e) of TRIA, as amended by the Terrorism Risk Insurance Extension Act of 2005, required the

President's Working Group on Financial Markets to perform an analysis and report to Congress regarding the long-term availability and affordability of insurance for terrorism risk, including group life coverage and coverage for chemical, nuclear, biological, and radiological events.

In September 2006, the President's Working Group on Financial Markets submitted a report to Congress on Terrorism Risk Insurance. That report can be accessed at <http://www.treas.gov/offices/domestic-finance/financial-institution/terrorism-insurance/pdf/report.pdf>. The report found that the availability and affordability of terrorism risk insurance had improved since the terrorist attacks of September 11, 2001, including that pricing for terrorism risk insurance had fallen and take-up (purchase) rates had risen. The improvement was due to several factors including better risk measurement and management, improved modeling of terrorism risk, increased reinsurance capacity, and the financial condition of property and casualty insurers. Still, the report also found that a significant number of policyholders were not purchasing coverage at that time. The report found that group life insurance (which is not included in the Program) remained generally available, that prices had declined, and that there had been improvements in the availability of catastrophic life reinsurance. The report concluded that there appeared to be little potential for future market development of terrorism risk insurance for losses associated with chemical, nuclear, biological, and radiological attacks.

In addition to extending the Program through 2014, the Terrorism Risk Insurance Program Reauthorization Act of 2007 amended Section 108 of TRIA to require an on-going analysis by the President's Working Group on Financial Markets regarding the long-term availability and affordability of insurance for terrorism risk generally. The President's Working Group on Financial Markets is required to submit a report to Congress in 2010 (and another report again, in 2013). The President's Working Group on Financial Markets is to conduct its analysis in consultation with the National Association of Insurance Commissioners, representatives of the insurance industry, representatives of the securities industry, and representatives of policyholders. This Notice seeks comment from these and any other interested parties as a means of satisfying the consultation

requirement in the most open and efficient manner.

### **I. General Solicitation for Comments About the Long-Term Availability and Affordability of Terrorism Risk Insurance**

Please comment generally; and please include data and other information in support of such comments, where appropriate and available, regarding the long-term availability and affordability of insurance for terrorism risk. All relevant views and comments are invited.

In addition, please consider providing comments in response to the following specific questions:

### **II. Specific Questions**

#### *Key Factors*

1. What are the key factors that determine the availability and affordability of terrorism risk insurance coverage? How are these factors being measured and projected today? What factors will determine the availability and affordability of terrorism risk insurance long-term? The President's Working Group on Financial Markets discussed various factors in its 2006 report, referenced above; how have these factors changed or developed since then?

2. What are the key factors that determine the amount of private-market insurer and reinsurer capacity made available for terrorism risk insurance coverage? How have these factors changed since 2006, when the President's Working Group on Financial Markets issued its last report? How will such factors evolve in the long-term and upon what factors will available capacity most depend?

#### *Economic Factors*

3. How, in general, has the state of the financial markets and economy, and the financial condition of commercial property and casualty insurers, affected the availability and affordability of terrorism risk insurance; and how does that compare with effects on the availability and affordability of other lines or types of commercial property and casualty insurance? Please comment on potential entry of new capital into, as well as any exits from, the terrorism insurance and reinsurance markets.

#### *Underwriting*

4. What changes and improvements have taken place in the ability of insurers to measure and manage their accumulation of terrorism risk exposures, and how (as well as to what extent) are primary insurers using

available methods? Has improved risk accumulation management led to more availability? Has there been any improvement in modeling of frequency and terrorist behavior? What has been learned from the near-9 years of experience in managing and assessing terrorism risk since September 11, 2001? Overall, how has modeling improved and/or continued to develop since 2006, when the President's Working Group on Financial Markets issued its last report? How is modeling expected to evolve further in the long-term?

5. What role do mitigation and loss prevention play in underwriting and pricing terrorism risk insurance? How has mitigation developed since 2002, what improvements have been made since 2006, to what effect has the availability of terrorism risk insurance had on mitigation and vice versa; and, how will mitigation evolve in the long-term?

6. What is the state of information sharing between and among the private and official sectors related to terrorism risk: (a) How much reliance is placed on open and private source intelligence; (b) how has it affected the availability and affordability of terrorism risk insurance; and, (c) how will such information processes further develop and affect the availability and affordability of terrorism risk insurance in the long-term?

#### Coverage

7. What changes and improvements have taken place with regard to the types of terrorism risk insurance coverage available in the market? What changes and improvements have taken place since 2006? Have there been improvements and changes in forms, are there special terms or conditions? What is the state of standalone, "TRIA-only" coverage? Is available coverage limited to, or broader than that required to be made available under TRIA?

8. What are the differences in availability and affordability of terrorism risk insurance coverage for foreign and domestic terrorist acts?

9. Did the Terrorism Risk Insurance Program Reauthorization Act of 2007's amendment to the definition of "act of terrorism" lead to more availability due to the requirement that such coverage be made available, or was such coverage available prior to 2007; conversely, did the amendment lead to less coverage due to the broadened scope of "act of terrorism" exclusions, or were exclusions revised to distinguish between coverage of foreign and domestic terrorist acts?

10. What are the differences in availability and affordability of

terrorism risk insurance coverage for losses at U.S. locations, as compared to such coverage for losses at non-U.S. locations? What are the differences as compared between TRIA-covered locations and non-TRIA locations?

#### Policyholder Demand

11. How has the demand for terrorism risk insurance changed since 2006, when the President's Working Group on Financial Markets issued its last report? Please comment on take-up by policyholder sector, location, line, and other relevant characteristics. How have any changes in demand influenced the willingness of insurers to allocate capital to terrorism risk insurance? Has there been any impact on the amount of capital allocated to non-terrorism coverage or among lines of insurance?

12. To what extent have businesses used captive insurance companies to provide terrorism risk insurance, and what is the potential for the use of captive insurers to insure against such risk long-term? How have stand-alone terrorism captives developed, and how will these evolve long-term, including after the expiration of the Program in 2014?

13. Have State approaches (such as those applicable to mandatory coverage, permitted exclusions, and rate regulation) made coverage more or less available and affordable? Have there been any changes in State insurance regulation of terrorism risk insurance since the Terrorism Risk Insurance Program Reauthorization Act of 2007 was enacted? To what extent has the availability and affordability of terrorism risk insurance been influenced by State insurance regulation, and what role is State regulation expected to have long-term? Please comment on State-approved terrorism related rate loads.

14. What are the differences in availability and affordability of terrorism risk insurance between the licensed/admitted market and the non-admitted/surplus lines market, and to what degree are those differences attributable to the degree and manner in which each market is regulated?

#### Price of Insurance

15. What improvements have taken place in the ability of insurers to price terrorism risk insurance? How are rating organizations assisting insurers in pricing, and how have rating factors developed?

16. What have been the trends in pricing of terrorism risk insurance? Please comment on the extent to which such coverage is not priced and charged-for. How has pricing changed since 2006, when the President's

Working Group on Financial Markets issued its last report? To what do you attribute any changes?

17. How has the recent "soft market" impacted the availability of and affordability of terrorism risk insurance? What would be the impact on the availability and affordability of terrorism risk insurance should the market "harden" in the near future?

18. How were primary insurers' pricing decisions affected by the Terrorism Risk Insurance Program Reauthorization Act of 2007, particularly as to the requirement to make available coverage for acts of terrorism being no longer defined as limited to those committed on behalf of any foreign person or foreign interest?

#### Reinsurance

19. What is the current availability and cost of reinsurance to cover terrorism risk? Please distinguish by line or type of insurance being reinsured and on what basis (treaty or facultative). How has the terrorism reinsurance market changed since 2006, when the President's Working Group on Financial Markets issued its last report? To what do you attribute any changes?

20. At what policyholder retention levels are insurance programs being structured by policyholders to cover terrorism risk (e.g., deductibles, self-insurance, captives); and, with regard to insurers, how are reinsurance programs being structured and at what attachment points? Please comment on the availability and affordability of reinsurance for terrorism risk.

21. Are reinsurers allocating more capital to terrorism risk insurance, and has capacity changed since 2006, when the President's Working Group on Financial Markets issued its last report? Are insurers willing to pay the cost of terrorism risk reinsurance, and is that a factor affecting the allocation of capital to the risk; how much additional capital could be attracted long-term?

22. How have provisions of the Terrorism Risk Insurance Program Reauthorization Act of 2007 affected the terrorism risk reinsurance market? More specifically, how has maintaining and not increasing the insurer deductible percentage applied against direct earned premiums (from Program lines), as well as not decreasing the Federal share of losses above the insurer deductible, affected the provision and development of private reinsurance?

23. To what extent have alternate risk transfer methods (e.g., catastrophe bonds or other capital market instruments) been successfully or unsuccessfully used for terrorism risk insurance, and what is the potential for

the long-term development of these approaches?

*Losses Associated With Chemical, Nuclear, Biological, and Radiological (CNBR) Acts*

24. What is the current availability and affordability of coverage for CNBR events? For what perils is coverage available, subject to what limits, and under what policy terms and conditions? Is there a difference in the availability and affordability of coverage for CNBR events caused by acts of terrorism? To what extent have various States allowed insurers to exclude coverage for CNBR events (Please comment on requirements for workers' compensation and fire-following coverage.)? How have exclusions developed?

25. Is it the case that some insurers appear unwilling to provide coverage for CNBR events caused by acts of terrorism, despite TRIA limits on an insurer's maximum loss exposure? If so, why?

26. In the long-term, what are the key factors that will determine the availability and affordability of terrorism risk insurance coverage for CNBR events? The President's Working Group on Financial Markets previously reported that there appeared to be little potential for market development. Has anything changed since 2006?

*Deductible and Co-Share Levels*

27. Under the Program, an insurer's annual deductible is a percentage of certain direct earned premiums (as defined by TRIA and regulation). TRIA, as originally enacted, graduated the percentage applied for each year. The Terrorism Risk Insurance Program Reauthorization Act of 2007 established a set percentage of 20 percent for each Program year beginning in 2007. Please comment for each year since 2006 as to whether direct earned premiums in TRIA lines and insurer deductibles have increased or decreased? If so, in what amounts? Please provide data as available.

28. How might any increases to the insurer deductible level or decreases to the Federal share above such deductible levels, prior to the Program's expiration in 2014, affect the availability and affordability of terrorism risk insurance? Please comment on the degree, amount or increment of any recommended increase.

*Expiration of the Program*

29. Describe efforts undertaken by the insurance industry and/or policyholders since 2006, when the President's Working Group on Financial Markets

issued its last report, to ensure the availability and affordability of terrorism risk insurance after 2014 when the Program expires, and long-term?

30. Please comment on any anticipated State approaches to ensure the continued availability and affordability of terrorism risk insurance after the Program expires in 2014 (such as those approaches taken by the States after September 11, 2001 and before TRIA was enacted on November 26, 2002).

31. Please comment on any other developments in markets that might affect the continued availability and affordability of terrorism risk insurance.

32. In the absence of the Program, in what forms, at what levels, under what terms and conditions, and at what price might terrorism risk insurance be available; and, at what duration (*i.e.*, long-term)? Please distinguish from State-mandated coverage, such as workers' compensation and fire insurance.

**Michael S. Barr,**

*Assistant Secretary of the Treasury.*

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**DEPARTMENT OF THE TREASURY**

**Office of Thrift Supervision**

**Deposits**

**AGENCY:** Office of Thrift Supervision (OTS), Treasury.

**ACTION:** Notice and request for comment.

**SUMMARY:** The proposed information collection request (ICR) described below has been submitted to the Office of Management and Budget (OMB) for review and approval, as required by the Paperwork Reduction Act of 1995. OTS is soliciting public comments on the proposal.

**DATES:** Submit written comments on or before July 19, 2010. A copy of this ICR, with applicable supporting documentation, can be obtained from RegInfo.gov at <http://www.reginfo.gov/public/do/PRAMain>.

**ADDRESSES:** Send comments, referring to the collection by title of the proposal or by OMB approval number, to OMB and OTS at these addresses: Office of Information and Regulatory Affairs, Attention: Desk Officer for OTS, U.S. Office of Management and Budget, 725 17th Street, NW., Room 10235, Washington, DC 20503, or by fax to (202) 395-6974; and Information Collection Comments, Chief Counsel's Office, Office of Thrift Supervision,

1700 G Street, NW., Washington, DC 20552, by fax to (202) 906-6518, or by e-mail to [infocollection.comments@ots.treas.gov](mailto:infocollection.comments@ots.treas.gov). OTS will post comments and the related index on the OTS Internet Site at [www.ots.treas.gov](http://www.ots.treas.gov). In addition, interested persons may inspect comments at the Public Reading Room, 1700 G Street, NW., by appointment. To make an appointment, call (202) 906-5922, send an e-mail to [public.info@ots.treas.gov](mailto:public.info@ots.treas.gov), or send a facsimile transmission to (202) 906-7755.

**FOR FURTHER INFORMATION CONTACT:** For further information or to obtain a copy of the submission to OMB, please contact Ira L. Mills at [ira.mills@ots.treas.gov](mailto:ira.mills@ots.treas.gov), (202) 906-6531, or facsimile number (202) 906-6518, Regulations and Legislation Division, Chief Counsel's Office, Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552.

**SUPPLEMENTARY INFORMATION:** OTS may not conduct or sponsor an information collection, and respondents are not required to respond to an information collection, unless the information collection displays a currently valid OMB control number. As part of the approval process, we invite comments on the following information collection.

*Title of Proposal:* Deposits.

*OMB Number:* 1550-0093.

*Form Number:* N/A.

*Regulation requirement:* 12 CFR Parts 557.20, 230.3, 230.4, 230.5 and 230.6.

*Description:* Section 557.20 requires savings associations to establish and maintain deposit documentation practices and records. These records should include adequate evidence of ownership, balances, and all transactions involving the account. In addition, part 557 relies on the disclosure regulations applicable to savings associations under Regulation DD. Regulation DD implements the Truth in Savings Act, part of the Federal Deposit Insurance Corporation Improvement Act of 1991.

The regulations assist consumers in comparing deposit accounts offered by depository institutions. Consumers receive disclosures about fees, annual percentage yield, interest rate, and other account terms whenever a consumer requests the information and before the consumer opens an account. The regulation also requires that savings associations provide fees and other information on any periodic statement the institution sends to the consumer. Regulation DD contains rules for advertisements of deposit accounts and