

4810-25-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: Department of the Treasury, Departmental Offices.

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 [INSERT DATE THAT IS 45 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

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, N.W., Washington, D.C. 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 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 ongoing 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 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.

Dated:

Michael S. Barr
Assistant Secretary of the Treasury