

RIMS has been at the forefront of the introduction, adoption and extension of the Terrorism Risk Insurance Act. Our members have testified before Congress, and we have brought our message personally to Capitol Hill. With this vital legislation set to expire on December 31, 2007, RIMS is proud to issue its "Position on a Long-Term Solution to Terrorism Exposure". We will continue to work closely with leaders in Congress, as well as industry partners to ensure that there continues to be a federal back stop to terrorism exposure in the United States beyond 2007.

POSITION ON A LONG-TERM SOLUTION TO TERRORISM EXPOSURE

Terrorism is one of the largest and least predictable catastrophic exposures for businesses. The Risk and Insurance Management Society, Inc. (RIMS), the largest association of risk managers in the United States, is very concerned about the fast-approaching expiration date of the Terrorism Risk Insurance Act (TRIA) on December 31, 2007 without any long-term successor program in place. Without the stability offered by a permanent long-term solution, our members are faced with an uncertain and costly marketplace that is not equipped to assist in the protection and sustainability of our country's assets. Accordingly, something must be done to ensure that terrorism insurance continues to be available to buyers of commercial insurance in a comprehensive and affordable manner once TRIA expires. Time is of the essence. RIMS is prepared and willing to work with public and private organizations to develop a solution or consensus opinion in order to have a unified approach before Congress.

There are a number of proposals that have been issued by the insurance industry and from representatives of the real estate and financial services markets. RIMS membership includes representatives of all of these industries, as well as businesses across the broad spectrum of the economy. Through ongoing discussions and polling of our membership, RIMS has identified critical factors that should form the foundation of any solution. Therefore, rather than endorsing a particular plan or developing one of our own, RIMS embraces four principles that we feel should underlie any plan that is adopted.

1. RIMS members believe that a private/public partnership provides the best alternative to addressing the long-term needs of availability and affordability of insurance to cover acts of terrorism.

While RIMS members' first choice would be a complete private market solution to cover acts of terrorism post TRIA, the last four years have demonstrated that the private insurance market alone will not be able to respond to provide adequate coverage for terrorism exposures. Acts of terrorism are too difficult to predict and are, therefore, too difficult to price. To be insurable, expected losses must be reasonably estimable, and terrorism losses simply do not fit this criterion. For this reason, the private market has not provided coverage without the federal government acting as a reinsurer of last resort. With federal government participation there is at least some level of certainty for private carriers in predicting their maximum exposure. Some form of risk pooling may be an appropriate approach. Also, financial incentives and eligibility for participation in the program should be considered to encourage creation of private insurance capacity. Regardless of the private market involvement, the federal government will likely be required to continue to be involved in a reinsurance capacity at some level with the scope of involvement possibly decreasing over time. Notwithstanding the statement from the President's Working Group on Financial Markets that TRIA legislation has prevented the emergence of new financial capacity for terrorism coverage, RIMS believes the opposite—that the capacity that is currently available is a direct result of TRIA. RIMS believes that absent some form of federal backstop, there will never be sufficient capacity available to cover those businesses that require the highest policy limits.

2. Any solution needs to address the long-term availability and affordability of insurance coverage for nuclear, biological, chemical and radiological (NBCR) events caused by terrorism.

The federal government has stated that potential acts of terrorism from these sources are likely. RIMS believes the NBCR risks represent some of the most problematic areas in the on-going TRIA debate. Currently, TRIA is silent on NBCR, meaning that if it is covered in the underlying insurance

contract then TRIA will respond. For workers' compensation insurance, carriers cannot exclude NBCR risks. Therefore, TRIA is critical to support this catastrophic exposure. In other lines such as property, it is common for insurers to specifically exclude coverage for NBCR meaning no coverage is available for these risks. This represents a major gap in coverage and RIMS believes this should be addressed going forward as the evaluation takes place for a long-term solution. The stand-alone terrorism insurance market continues to be extremely limited in that it really only exists for property lines of coverage. It is very limited in terms of its capacity and price, and there is virtually no coverage available for NBCR risks.

In its September 2006 report on insuring NBCR risks ("Terrorism Insurance, Measuring and Predicting Losses from Unconventional Weapons is Difficult, but Some Industry Exposure Exists"), the GAO notes that "[i]nsuring NBCR risks is distinctly different from insuring other risks because of the potential for catastrophic losses, a lack of understanding or knowledge about the long-term consequences, and a lack of historical experience with NBCR attacks in the United States." Insurers face distinct challenges when it comes to measuring and predicting NBCR risks because they generally fail to meet commonly accepted principles of an insurable risk. Accordingly, the GAO concluded that, "[g]iven the challenges faced by insurers in providing coverage for, and pricing, NBCR risks, any purely market-driven expansion of coverage is highly unlikely in the foreseeable future."

3. RIMS believes that all commercial property, workers' compensation, and liability lines should be included in any new plan.

As a reinsurance backstop, TRIA has opened commerce by quantifying the maximum loss exposure so that insurers and reinsurers can offer workers' compensation, property and liability coverage prudently. With maximum possible losses somewhat quantifiable, insurers and reinsurers can offer commercial insurance to companies, both public and private, that need terrorism coverage. Prior to

the enactment of TRIA, and after the January 1, 2002 expiration of most reinsurance treaties, the required supply of commercial insurance coverage for acts of terrorism was not available.

4. RIMS believes that insurance companies writing commercial lines should be required to participate in the program and be required to make coverage available for acts of terrorism.

Having adequate insurance coverage for U.S. businesses is important to the economic well-being of the nation. Without TRIA or a viable permanent substitute, RIMS believes, insurance companies will review their portfolios of business and will refuse to continue covering certain risks and areas where they are overexposed. We believe this will be true for workers' compensation, property and even third party liability lines of coverage. It will affect all businesses both large and small. Such reductions in the supply of coverage available could result in a significant national economic crisis. Many businesses in the United States rely on global insurance companies for coverage. These insurers decide where to underwrite risk based on their assessment of overall profitability and return to their shareholders. If the risk to write coverage is perceived to be too great, U.S. companies will be left without the coverage they need to operate.

Conclusion

RIMS has been directly involved in the creation and extension of TRIA, and looks forward to continuing to work with public and private organizations to ensure that terrorism insurance remains available and affordable for U.S. companies. Unless other market-driven alternatives are developed, many of the over 4,000 commercial policyholders that RIMS represents will experience exorbitant property, workers compensation and liability insurance rates for significantly less coverage, if it is available at all. Businesses may experience a complete loss of protection from terrorist acts, as a result of insurance companies' inability to obtain reinsurance protection. Time is of the essence to develop a

long-term solution. Without a solution in place by December 31, 2007, the Country faces a potential catastrophic exposure to the economy.

December 7, 2006

