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**Chairman Baker, Chairwoman Kelly, Ranking Member Kanjorski, Ranking Member Gutierrez and Members of the Subcommittees,**

Thank you for the opportunity to appear before you today to provide my insight on a singularly important issue before our country and our economy in the post 9/11 world: How should we manage terrorism risk effectively and fairly?

My objective today is to convey a simple, fundamental message: **terrorism is a unique peril because it is a public risk and not privately insurable without a federal backstop.** Right now it presents an insurmountable challenge for the private markets alone to understand or manage. Hence, terrorism risk can only be managed effectively and fairly in partnership with the federal government. The insurance industry has always played a critical role in the U.S. economy, and we will continue to do so. But the potential risk of a large scale terrorist event is beyond the resources of our industry.

As our nation's second oldest insurer, we at The Hartford pride ourselves on having been there for our policyholders when they've needed us for almost two hundred years. Policyholders from Abraham Lincoln to Babe Ruth have relied on us to fulfill our promise to meet our obligations to them. We were there during the Great Chicago Fire, and the 1906 San Francisco earthquake. We were there on 9/11.

**As I survey The Hartford's 196-year history and my own experience in this industry for more than three decades, I see no other peril quite like terrorism.** Here's why:

**Terrorism is a unique risk**

One characteristic that makes terrorism unique is that it is a public risk. Our government's leaders and leading terrorism experts have described it as the 21st century's version of war. Terrorist attacks are explicitly designed to threaten our national security. They target the entire country and our government, no matter where they occur or who they harm or kill.

Terrorism is also a public risk given the magnitude of potential attacks on the entire economy.  The American Academy of Actuaries has published insured loss estimates for attacks on select U.S. cities using nuclear, biological, chemical or radiological weapons (NBCR).  For a large NBCR attack on New York City that estimate totals $778 billion.  A similar NBCR event in Washington, D.C. would result in an insured loss of almost $200 billion; in San Francisco it could cause an insured loss of $171 billion.  Even a medium NBCR event could trigger $446 billion in insured losses in New York City, $106 billion in Washington, D.C. and $92 billion in San Francisco.  A terrorist attack employing a suitcase nuclear device in an urban area will far exceed the private insurance market's capacity to manage it. The capital of the entire P&C industry is $427 billion, and much of this is devoted to products which bear minimal risk to terrorism losses.

For a national carrier like The Hartford, reinsurance capacity for certified terrorism losses on property coverage ranges from extremely limited to non-existent.  For example, The Hartford's 2006 retention under the Terrorism Risk Insurance Extension Act (TRIEA) is just over $1 billion.  Within this TRIEA retention, reinsurance protection against property losses from certified terrorism events is effectively unavailable.  In contrast, for natural catastrophe losses, The Hartford's principal catastrophe reinsurance treaty alone provides more than $600 million in coverage for individual loss events in excess of a $175 million retention.  Nothing in TRIEA today is preventing the markets from providing reinsurance coverage within our retention, like they do for natural catastrophes. The market appetite hasn't appeared in any significant way.  Why? The problem is the uninsurable nature of this peril.

**Terrorism is uninsurable**

As a risk, terrorism is also unique because it is uninsurable.  In private insurance markets, efficiency is achieved by ensuring that the premium charged for each policyholder is based on the amount of risk that each policyholder contributes to the overall pool.  In other words, we align costs with responsibility.  Private insurance works properly only when insurers have the ability to effectively pool the loss experience of policyholders exposed to relatively *homogeneous*, *random* and *independent* risks, and where the underlying sources of risk are *well understood* and, therefore, appropriately priced.

The problem with terrorism is that it fails each of the prerequisites for insurability.

First, the risks are not homogeneous.  The risk of terrorism to any one location may vary greatly by such factors as geographical location, industry, company reputation, and level of defensive preparation.  Adding to the problem is the fact that these factors may change over time.

Second, the risks are by definition not random. Unlike storms or car accidents, terrorist attacks involve the purposeful, coordinated selection of targets based on the terrorists' objective of inflicting maximum potential damage to the economy.

Third, terrorism risks are not independent. Terrorism experts and federal officials have identified a large number of plausible terrorism scenarios that could involve losses of such a large scale that the attack would simultaneously impact a large proportion of any insured portfolio.

Finally, the risks are not well understood. Unlike other catastrophe risks like hurricanes and earthquakes, where a tremendous amount of data is available on the probability and severity of loss events, no credible data or models exist to price or manage the risk of terrorism. Absent information necessary to understand the probability of a terrorist attack, the risk cannot be priced, and therefore remains uninsurable. The risk cannot be priced. Without the ability to price, no market for terrorism risk will form.

**We Do Not Operate in a Free Market**

It is helpful to keep in mind the operating environment of primary insurance carriers like The Hartford. Our market is carefully regulated by each of the 50 states, and we must often receive permission from state regulators to enter a state, design a product for sale and the price for which to sell it. Insurers also often need to secure approval to stop covering a peril or quit writing this business altogether. As our private reinsurance has evaporated after 9/11, we have been vigilant to ensure that some public backstop remains in place. Without private reinsurance and without federal terrorism coverage, individual insurers may have no choice but to leave an entire section of the market, and, sometimes, a state, altogether – an outcome that we in the industry do not believe it in the best interest of our policyholders.

This is especially the case for workers compensation insurance, where the insurer is responsible for covering a loss, regardless of how a worker dies – including by a terrorist-delivered weapon. Since workers compensation is a statutory policy, state regulators could not delete terrorism coverage even if they chose to.

Lastly, state regulators also decide how much insurance companies may charge for premiums, including terrorism. Even if we had a reliable way to price terrorism, it would be up to each state to decide whether or not we could charge that amount. Consequently, insurers might receive a "market" rate from reinsurers and other suppliers of capital, but our rates to our customers are strictly regulated and often restricted.

In contrast, the reinsurance companies we work with to manage our risks operate under different rules which allow them much greater flexibility. Reinsurers, like primary insurers, understand that terrorism is uninsurable. Unlike primary insurers, reinsurers had the option to stop covering the terrorism peril, so after 9/11, they have largely withdrawn from the market.

**Role for the U.S. Government**

Given these factors, one fact stands out: managing terrorism risk successfully requires a public/private partnership. Nearly every civilized country that has been the victim of repeated terrorist attacks has accepted this risk as a public one. Either the government bears the risk alone or in concert with the private market. The United Kingdom, Spain, South Africa, Australia, Israel, France, Germany, the Netherlands, India and Pakistan all have some form of government backing to facilitate insurance coverage for terrorism.

The United States has been no exception. In the wake of 9/11, the Congress passed the Terrorism Risk Insurance Act (TRIA), and last year it extended this program through 2007. TRIA has been shown thus far to be a successful partnership between the federal government, insurers and policyholders to protect the economy in the event of an attack.

Of course, in the U.S., terrorism is not the only peril that has been managed by a partnership between the government and the private sector. Aviation accidents, nuclear mishaps, floods and riots have all prompted similar public/private partnership arrangements. In addition, through the Overseas Private Investment Corporation, our government provides terrorism coverage for U.S. companies' overseas operations.

**A solution must be long term**

As a nation, we can take some comfort in the fact that since 9/11, terrorists have not succeeded in attacking U.S. interests on our own soil. Still, other countries in the world have been less fortunate. We should listen to and act on the judgment of our most senior government leaders. They constantly remind us that the risk of terrorist attacks in the U.S. remains high and that this risk will be with us for many years to come.

The inescapable conclusion is that as long as this terrible risk threatens our way of life, we need to have a way to fortify our economy against it. The insurance industry is willing to play an integral role to finance this risk, working together with policyholders and the government, but we cannot do it alone.

**Work Continues on a Long Term Solution**

The Hartford is willing and eager to work with any group of interested parties on finding a permanent solution. Indeed, I have collaborated with the companies and associations on today's panel. And I have visited with many of you and your colleagues in the Senate over the past 5 ½ years as you have developed TRIA and TRIEA. We have spent considerable time and energy ensuring that the two Acts work and trying to construct a long-term solution which will work for all. I cannot say that we have "cracked the code" yet.

As we continue this work, I believe that the following principles must necessarily be part of the answer:

- Our Federal Government must play a role, including, if necessary, preempting any state impediments to a workable national solution;
- Congress needs to give special attention to the terrorists' new and horrific tools of war; and,
- The solution must last as long as the threat of terrorism does.

Thank you.