

THE TRUTH ABOUT TERRORISM INSURANCE:
WILD CLAIMS BY BUSINESS LOBBYISTS DON'T HOLD UP UNDER SCRUTINY

Contact: J. Robert Hunter 703-528-0062; Travis Plunkett 202-387-6121

Business interests have made a number of alarming claims to support their contention that the lack of action on terrorism insurance legislation has harmed the economy. **These lobbyists are obviously concerned that a fast-developing private market for terrorism insurance has made broad federal intervention increasingly unnecessary.** When examined closely, the terror insurance “facts” offered by industries that stand to benefit from this legislation start look more like gross exaggerations, half-truths and, in some cases, outright lies. For example, in an October 2nd advertisement in the Washington Post, the American Insurance Association, Business Roundtable and U.S. Chamber of Commerce contended that “there is too much at stake” to not pass terror insurance legislation. Not a single claim about terrorism insurance made in this ad holds up under scrutiny:

MYTH: 300,000 jobs have been “left wanting by the lack of terrorism insurance legislation” (Real Estate Roundtable). “Nearly \$4 billion in job-enhancing construction projects have been killed” (Mortgage Bankers Association of America).

FACT: 300,000 jobs would represent a whopping 5.5% of all non-residential construction jobs.¹ \$4 billion in construction would represent 1.9% of all projects.² News reports and insurance sources indicate that the only sector with persistent (but limited) terror insurance problems is high-end real estate, not new construction.³ It is simply not believable that so many projects have been killed and jobs lost. According to the Federal Reserve Board, the lack of federal terror backup has not led to a lending slowdown,⁴ which is how these construction projects would die. How is it possible that so many construction projects have been killed and jobs lost if financing is largely available?

Moreover, the organizations that have made these wild estimates have not listed specific construction projects that have been cancelled solely because of the lack of terrorism coverage, making it impossible to confirm their accuracy. An unverifiable claim doesn't pass the “laugh test.” As the Christian Science Monitor editorialized last week, “...there's very little evidence that developers, banks, and the real estate industry are holding back investments because of lack of terrorism coverage, instead of just a sluggish economy. President Bush's claim that some \$15 billion worth of construction

¹ There were 6,201,600 construction jobs in 2000, which includes 741,600 residential construction jobs. Statistical Abstract of the United States, U.S. Census Bureau, 2001. There have not been claims that residential construction has been in any way impacted by the terrorist attacks. Thus, 300,000 jobs would represent 4.8% of all construction jobs and 5.5% of all non-residential construction jobs.

² The value of non-residential construction in 2000 was \$210 billion, Ibid.

³ “How the Lack of Federal Back Up for Terrorism Insurance Has Affected Insurers and Consumers: An Update,” Consumer Federation of America, August 22, 2002, “How the Lack of Federal Back Up for Terrorism Insurance Has Affected Insurers and Consumers: An Update,” Consumer Federation of America, August 22, 2002, http://www.consumerfed.org/terror_insurance_report.pdf.

⁴ The April 2002 Senior Loan Officer Opinion Survey on Bank Lending Practices, Board of Governors of the Federal Reserve System.

projects and some 300,000 jobs are in jeopardy doesn't hold up. The construction industry, after all, is a \$4 trillion business, and it's difficult to pinpoint reasons for its ups and downs.”⁵

MYTH: “*More than \$15 billion in real estate transactions have been canceled or delayed*” (Real Estate Roundtable).

FACT: There is a lot of evidence that terrorism insurance is widely available.⁶ Since the beginning of the year, malls, sports stadiums, airlines, construction contractors and even the Sears Tower and World Trade Center clean-up site have gotten coverage. Some very high-value buildings are having trouble finding coverage in New York, Chicago, and, to a lesser degree, Washington D.C. This is especially true above the \$500 million to \$1 billion in stand-alone coverage that all but the most risky buildings can obtain. However, the problem is limited in scope.⁷

Thus, the \$15 billion number appears to have been pulled out of thin air. Once again, the organization behind it has not detailed the specific buildings that can't obtain coverage. Since when does Congress pass legislation to benefit a particular industry without verifying the extent of the problem?

MYTH: “*Sixty-five percent of companies have no coverage at all for terrorism*” (Risk and Insurance Management Society).

FACT: This is an outright lie. RIMS did not look at all companies to determine whether coverage was available. They only surveyed their members; the “jumbo risks” that are the most difficult and expensive to insure. Insurance sources report that the vast majority of businesses in America have terror coverage. Travelers Insurance, for example, has stated that it writes terror coverage routinely for businesses with premiums below \$1 million.⁸ This represents the vast majority of all businesses getting the coverage routinely. No one claims that small or mid-sized businesses can't secure terror coverage at reasonable prices today. For example:

...for writers of small and medium-size risks, it's really business as usual. Underwriting hasn't changed since last September, because the maximum loss from a small business doesn't change if the loss results from a terrorist's bomb or a hurricane. While

⁵ “Insurance and Terrorism,” Christian Science Monitor, October 4, 2002.

⁶ “Statement Number 182,” The Shadow Financial Regulatory Committee, An independent committee sponsored by the American Enterprise Institute, September 23, 2002. Among other things, the Committee concludes, “... the dire predictions of many observers have not come to pass. Insurers and reinsurers have raised over \$30 billion in new capital with at least another \$10 billion in new issues pending. Although primary insurers excluded terrorism coverage from their basic commercial property programs in the large majority of states that approved such exclusions, separate stand-alone coverage initially became available with total limits in the \$250 million range. Limits as high as \$1 billion are now available, and further increases in available limits are likely. While the prices of coverage are often high, the insurance brokerage community estimates that prices have declined by 50 to 75 percent since early in 2002, indicating that the market is adjusting. The availability of separate, stand-alone reinsurance for terrorism losses also has expanded since that time. Several catastrophe-modeling companies have developed, or are developing, models for use in forecasting terrorism losses, which should help insurers and reinsurers price and manage the risk....“The insurance, reinsurance, and lending markets have clearly made substantial progress in digesting the events of last September. In conclusion, private insurance, reinsurance, and lending markets have made and are continuing to make substantial progress in adjusting to the post-September 11 world. Given those developments, the case for a federal backstop for terrorism insurance, which was not clear-cut late last year, is certainly less compelling now.”

⁷ “How the Lack of Federal Back Up for Terrorism Insurance Has Affected Insurers and Consumers: An Update,” Consumer Federation of America, August 22, 2002, http://www.consumerfed.org/terror_insurance_report.pdf.

⁸ “A Year After Terror, Commercial Insurers Look Closer at Concentrations of Risk”, BestWire, September 12, 2002.

underwriters might consider landmark buildings a greater risk because of the potential for future terrorist attacks, the risk on most average buildings hasn't changed... "I may look at the Sears Tower differently today, but I'm sitting in a tall office building myself, and I wouldn't underwrite it any differently than I did before Sept. 11," Gage [Travelers Insurance Executive] said. She said her division of Travelers doesn't write buildings the size of the Sears Tower, which would likely seek coverage on a layered basis... For these smaller accounts, with premiums less than \$1 million annually, Travelers doesn't impose blanket exclusions of terrorism coverage, Gage said.⁹

Even in the real estate area, the most adversely affected by lack of terror coverage, three-fourths of the businesses have it.

In its continuing efforts to clearly identify problems with the availability of terrorism insurance, the Building Owners and Managers Association (BOMA) International today released the results of its national survey on terrorism insurance coverage... more than one quarter of survey respondents were unable to obtain terrorism insurance... the remaining 73 percent who have been able to secure coverage...¹⁰

If the three out of four of the small number of businesses that have been the hardest hit by the terror insurance problem have coverage, it is simply impossible that 65% of all businesses do not have it.

Several very recent developments in the terror insurance market auger well for even more terror coverage in the future:

1. The insurance industry is now using three different computer models to predict the likelihood of terror attacks and to price coverage.

On Tuesday, [Helen Clark] plans to formally announce that AIR, a unit of Insurance Services Office Inc., which collects data for the insurance industry, has completed its terrorism project. It has solved the puzzle in part by using an approach developed during the cold war that turns educated guesses into numerical rankings that are cranked into a computer to determine risk... In fact, AIR has already sold its work, in the form of a computer model, to two insurers.¹¹

2. In part because of the new models, we now know that, for the first time, even the reinsurance market is returning for terrorism insurance.

MONTE CARLO, Monaco -- Reinsurers are still unwilling to offer comprehensive coverage for terrorism exposures, but, for a price, several are offering limited capacity for such risks. The recent introduction of computer-based terrorism models, a modified approach to underwriting the coverage and the high price charged has encouraged some reinsurers to offer stand-alone coverage.¹²

⁹ Ibid.

¹⁰ PR Newswire, Sept. 20, 2002.

¹¹ "The Race to Predict Terror's Costs," New York Times, September 1, 2002.

¹² "Terrorism reinsurance available-for the right price," Business Insurance, Sept. 23, 2002.

MYTH: “*Nearly \$7 trillion in commercial real estate debt is at increasing risk.*” (Insurance Information Institute). “*Commercial mortgage-backed securities are being downgraded because of the lack of terrorism insurance legislation*” (Moody’s Investors Service).

FACT: Of all the real estate in the country, a grand total of 14 properties have been downgraded by two ratings agencies (but not Standard and Poors). Fitch identified 13 properties it intended to downgrade some months ago, but only downgraded three because the other properties found terror coverage. Moody’s acted recently on 11 properties. There is a very good chance this small number of downgrades will be lifted as the properties secure the requisite coverage. Again and again, properties that have initially reported problems procuring terror coverage have found it, such as the Mall of America.¹³ As a result, it is virtually impossible that \$7 trillion in debt is “at risk.”

MYTH: A bill is needed “so that hard hats in America can get back to work.” (President Bush)

FACT: As stated above, there is no evidence that the lack of terror coverage has led to a serious construction slowdown, or loss of jobs. On the other hand, there is evidence that the legislation that is being considered would provide a financial windfall to insurers. The Senate terror insurance bill, which the President supports, provides insurance companies with reinsurance that is virtually free. Taxpayers would pick up 80 to 90 percent of all terror losses, after a very small initial deductible paid by insurance companies, up to \$100 billion. This would, overnight, decrease the financial exposure of insurance companies for existing terror policies and provide them a huge windfall, because the neither the Senate nor the House bill requires insurers to offer rebates for excessive premiums. Compare this approach to how Congress reacted to a previous insurance crisis, during the riots of the late 1960s. Insurers were charged a reinsurance premium for exposing the taxpayer to the risk of selling riot reinsurance. Taxpayers actually earned a profit.

¹³ The Mall of America obtained coverage early in 2002. Since then, trade journals have contained numerous reports like this: “Hilton Hotels Corporation said it’s resolved a dispute with the servicer of \$490 million in mortgage bonds by buying terrorism insurance...”, BestWire, September 9, 2002.